Washington State Legislature

Joint Committee on Pension Policy

2000 Interim Issues

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Washington State Legislature

Joint Committee on Pension Policy

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JOINT COMMITTEE ON PENSION POLICY
2000 Meetings and Issues

(December 1, 2000)

May 25, 2000

10 AM - 12:30 PM
House Hearing Room A, Olympia

1. **Committee Business**
2. **WSP System Report**
3. **Uniform COLA and Gain Sharing**

June 21, 2000

10 AM - 12:30 PM
House Hearing Room A, Olympia

1. **WSP System** — Roundtable
2. **LEOFF 1 Medical Expenses** — Roundtable

July 19, 2000

9:30 AM - 12:30 PM
Bldg. 2, Highline Community College, Des Moines

1. **TRS 1 30-year Cap and TRS 1 Post-retirement Employment** — Roundtable
2. **LEOFF 1 Medical Expenses** — Roundtable

August 16, 2000

9:30 AM - 1 PM
Room 407, CWU SeaTac Center
450 S. 142d St., SeaTac

1. **Public Safety Benefits** — Roundtable
2. **PERS 1 30-year Cap and Post-retirement Employment** — Roundtable
3. **Status of Pension Funds**
4. **How Rates Are Set**

September 20, 2000

9 AM - 12:30 PM
House Hearing Room A, Olympia

1. **Pension Funding Council**
2. **LEOFF 1 Medical Expenses** — Roundtable
3. **30-year Cap/Post-retirement Employment** — Roundtable
4. **Community College Litigation**
5. **LEOFF 1 Survivor Benefits for Post-retirement Marriage**

October 18, 2000

9:30 AM - 12:30 PM
House Hearing Room B, Olympia

1. **Pension Funding Council**
2. **Optional Plan 2 or 3 for TRS & SERS** — Roundtable

October - Continued

3. **SERS Transfer Payment**
4. **Uniform COLA at Age 66**
5. **LEOFF 1 Survivor Benefits for Post- retirement Marriage**
6. **LEOFF 1 Medical Expenses**

November 15, 2000

9 AM - 12:30 PM
House Hearing Room A, Olympia

1. **TRS 1 30-Year Cap**
2. **TRS 1 Substitutes**
3. **PERS Post-retirement Employment**
4. **Uniform COLA at Age 66**
5. **LEOFF 1 Survivor Benefits for Post-retirement Marriage**
6. **Housing Authority**
7. **SERS Technical Corrections**
8. **LEOFF Disability Age Tech. Corrections**
9. **Washington State Patrol**
10. **Optional Plan 2 or 3 for TRS & SERS**
11. **LEOFF 1 Medical Expenses**
12. **Public Safety Benefits**

December 13, 2000

9 AM - 1 PM
House Hearing Room A, Olympia

1. **Committee Business**
2. **Uniform COLA at Age 66**
3. **PERS 1 30-Year Cap**
4. **TRS 1 30-Year Cap Baker**
5. **Optional Plan 2 or 3 for TRS and SERS**
6. **SERS Correcting Amendments**
7. **LEOFF 2 Disability Age Corrections**
8. **Housing Authority**
9. **LEOFF 1 Survivor Benefits for Post-retirement Marriage**
10. **Washington State Patrol**
11. **LEOFF 1 Medical**
12. **Post-retirement Employment**
13. **DRS' Request ERBB/SIB**
14. **LEOFF 1 Survivor Benefits for Pre-retirement Divorce**
15. **Other Business**

2000 Interim Issues

Table of Contents

DRS' Request ERBB/SIB

Background:

The Department of Retirement Systems and the State Investment Board brought this request for recommended legislation before the Joint Committee on Pension Policy.

Committee Activity:

Presentation: SERS Technical Corrections
November 15, 2000, Full Committee Meeting
Proposal Approved:
December 13, 2000, Full Committee Meeting

Recommendation to Legislature:

Increases the membership of the Employee Retirement Benefits Board (ERBB) from eleven to twelve by adding a representative of deferred compensation program participants. The trustees for the deferred compensation accounts is changed from the State Investment Board to the ERRB, and definitions on statutory duties for record-keeping in the Plan 3 member accounts are added.

Staff Contact:

David Pringle – 586-7616 – pringle_da@leg.wa.gov

DRS' Request ERBB/SIB
Bill Summary

Department of Retirement System's Bill - Employee Retirement Benefits Board and State Investment Board Composition and Duties.

This language was suggested to the Joint Committee on Pension Policy by the Department of Retirement Systems.

The membership of the Employee Retirement Benefits Board (ERRB) is increased to twelve by adding a member representing the deferred compensation program participants.

The trustees of money in the state deferred compensation accounts and in the TRS, SERS, and PERS plan 3 individual member accounts are changed from the State Investment Board to the ERRB.

Housing Authority

Background:

The Everett Housing Authority created a small program in conjunction with local trade union halls to train some residents in construction skills while working on housing authority properties. The trainers and trainees in the housing authority program are required, along with their employer, to make retirement contributions to both the union-sponsored plan and PERS.

Committee Activity:

Presentation: Housing Authority
November 15, 2000, Full Committee Meeting
Proposal Approved:
December 13, 2000, Full Committee Meeting

Recommendation to Legislature:

Persons first employed exclusively as trainers or trainees in Housing Authority resident training programs after the effective date of the bill are excluded from PERS membership if they belong to a union-sponsored retirement plan.

Staff Contact:

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Housing Authority
Bill Summary

Background:

The Everett Housing Authority has a program to train some residents in trade skills. In conjunction with local trades union halls, a plan was launched that employed a program supervisor, two trainers, and three resident trainees in an apprentice-like system to gain trade skills working on renovation projects at Housing Authority properties.

The resident training program contract between the Housing Authority and the unions require a Journey level trainer for each resident trainee, and employer contributions to the union benefit plans of between 35 and 45 percent of the annual wages of each employee (not including Medicare and other payroll deductions). Membership in the Public Employees Retirement System is also required of both trainers and trainees, which requires a contribution of about two percent of pay by members and about four and one half percent by employers.

An exemption from PERS exists for apprentices in state-approved apprenticeship programs authorized according to chapter 49.04 RCW. Most Housing Authority trainees are not in approved programs, however, and the existing PERS exemption does not cover employees like the trainers in the Housing Authority program.

Summary:

Creates an exemption to PERS membership excluding individuals employed exclusively as trainers or trainees in a housing authority resident training program if the individuals are contributing members of a union-sponsored retirement plan.

The bill is prospective-only in approach, so that only individuals who have not been members of PERS prior to the effective date of the bill are exempted from PERS membership.

FISCAL NOTE

REQUEST NO.

RESPONDING AGENCY:	CODE:	DATE:	BILL NUMBER:
Office of the State Actuary	**035**	**11/06/00**	**Z-0240.3/01**

SUMMARY:

This bill impacts the Public Employee's Retirement System (PERS) by excluding from membership trainers or trainees in the resident apprentice training programs operated by housing authorities if they participate in a union sponsored or Taft-Hartley retirement plan.

Effective Date: 90 days after session.

MEMBERS IMPACTED:

This effects potentially new members by excluding them from PERS. The number of members in these positions is assumed to be rather small.

FISCAL IMPACT:

There is no fiscal impact.

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Gerald B. Allard, State Actuary

LEOFF 1 Medical Expenses

Background:

The JCPP submitted a report on LEOFF 1 medical benefits in 1995 which concluded that LEOFF 1 employers, as a whole, were not severely impacted by medical costs, particularly nursing home costs. In 1999, the employers sought another study of these medical benefits. The Legislature agreed to this by directing two studies: (1) a study of costs by the Office of the State Actuary as done in 1995; and (2) a study by the JCPP *"of the options for providing partial funding of law enforcement officers' and fire fighters' retirement system plan 1 retiree medical expenses from the surplus assets of the law enforcement officers' and fire fighters' retirement system plan 1 fund. The study shall include. . . a review of legal issues, federal tax compliance issues, variations in local government benefits and funding mechanisms, and other relevant issues."*

Committee Activity:

Presentation and Roundtable Discussion:
June 21, 2000, JCPP Full Committee Meeting
Presentation and Roundtable Discussion:
July 19, 2000, JCPP Full Committee Meeting
Presentation and Roundtable Discussion:
September 20, 2000, JCPP Full Committee Meeting
Presentation:
October 18, 2000, JCPP Full Committee Meeting
Presentation:
November 15, 2000, JCPP Full Committee Meeting
Presentation - Proposal Approved:
December 13, 2000, JCPP Full Committee Meeting

Recommendation to Legislature:

It is recommended that a risk pool be established whereby LEOFF 1 employers may jointly participate to spread the financial risks of unanticipated medical and nursing home costs for retirees by reimbursing costs not covered by insurance. Their participation would require payment of premiums. At the same time, the state would take advantage of federal law which allows for the transfer of excess retirement funds to a medical account for the benefit of retiree medical costs. Any funds the Legislature may desire to transfer would be used as a direct reimbursement to participating LEOFF 1 employers for health insurance premiums or as a contribution to the risk pool account.

The risk pool will be subject to state oversight, subject to the rules and regulations of the Office of the Risk Manager, Department of General Administration.

The Office of Community Development, Department of Community, Trade and Economic Development, will be designated as the operating agency for the risk pool and as the pass-through agency for the funds going directly to LEOFF 1 employers.

Staff Contact:

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LEOFF 1 Medical Benefits

Joint Committee on Pension Policy
December 28, 2000

Prepared by:

Gerald B. Allard
State Actuary

Introduction:

The 1999 Legislature directed the Office of the State Actuary to perform two studies of the Law Enforcement Officers' and Fire Fighters' Plan 1 (LEOFF 1) medical benefits. The first one required an actuarial study of local government liabilities for the retiree medical benefits required in chapter 41.26 RCW. The result of this is found in a separate report, Law Enforcement Officers' and Fire Fighters' Medical Services Benefit Report.

The second study directive, and the basis of this document, is found in Chapter 1, Section 908, Laws of 2000, 2nd Extraordinary Session:

> *"The joint committee on pension policy shall provide for a study, through the office of the state actuary during the 2000 interim, of the options for providing partial funding of law enforcement officers' and fire fighters' retirement system plan 1 retiree medical expenses from the surplus assets of the law enforcement officers' and fire fighters' retirement system plan 1 fund. The study shall include. . . a review of legal issues, federal tax compliance issues, variations in local government benefits and funding mechanisms, and other relevant issues."*

This report is in response to this legislative directive. It will outline the findings and recommendations of the Joint Committee on Pension Policy (JCPP).

The liabilities of local government LEOFF 1 medical benefits and funding, and other relevant issues are covered within the Law Enforcement Officers' and Fire Fighters' Medical Benefit Report.

The JCPP devoted several meetings to the LEOFF 1 medical issue and the concepts of the recommended plan. The specific JCPP meeting dates and the subject matter were as follows:

- June 21, 2000: An overview of the LEOFF 1 medical problem with a roundtable discussion.
- July 19, 2000: A continued overview of the LEOFF 1 medical problem with a roundtable discussion.
- September 20, 2000: A review of the legal issues and a conceptual proposal with a roundtable discussion.
- October 18, 2000: A review of LEOFF cashflows and flow chart of the conceptual proposal .
- November 15, 2000: Continuation of the conceptual proposal with a roundtable discussion.

- December 13, 2000: Presentation of proposed draft legislation for JCPP approval.

The roundtable discussions included representatives of active and retired LEOFF 1 organizations and representatives of the cities, counties and fire protection districts.

Recommendation Summary:

The recommendation addresses two issues:

- the difficulty of insuring certain required medical expenses. The primary benefit in this area is long term care but also includes some medical costs that are not usually covered by insurance policies; and
- the general cost of local government providing post-retirement medical care to LEOFF 1 members.

LEOFF 1 Surplus Assets:

LEOFF Plan 1 has surplus assets. This means that the latest actuarial valuation has determined the plan has more assets in the fund than are needed to pay all the future pension benefits.

The recommendation is to use the surplus assets to assist local government in paying the statutorily required medical benefits for LEOFF 1 retirees. This will be accomplished by following rules and procedures of the federal agency that regulates pension funds (IRS). The process only allows the use of surplus funds and requires the funds can only be used to provide medical benefits for LEOFF 1 retirees.

Long Term Care:

Medically necessary long term care is a required benefit for LEOFF 1 retirees. This is a very risky benefit. It has a relatively low incidence of occurring and may have a very high cost when it does occur. Private insurance is not available to cover all retirees.

The proposal is to create a medical benefits risk pool for LEOFF 1 employers. This would allow them to choose to share and, thereby, minimize the risk of financial loss due to long term care and those major medical costs not otherwise covered by medical insurance. This pool is proposed to be structured to operate on employer premiums alone. Surplus monies could be transferred from the LEOFF 1 retirement fund to assist local government with the premiums when IRS rules permit.

Medical Costs:

Medical costs are usually covered by local government insurance arrangements. The proposal is to reimburse local government for some of the retiree medical insurance premiums from the LEOFF 1 surplus when IRS rule permits.

Legal Issues:

State Law: One of the first tasks in the study concerned the legal aspects of assisting local governments with "excess" retirement or pension assets. It is apparent this topic moves into uncharted waters as it bears on state law. The subject was reviewed and other persons who are involved with retirement law were approached for their opinions. What was found is simply this: statutes and court decisions do not explicitly address using pension funds for medical benefits. Further, it is unknown how courts would apply legal precedents to this use of pension funds.

Federal Law: The Federal Internal Revenue Code (IRC) provides mechanisms for qualified pension plans to use surplus pension assets for the payment of medical services and insurance for retired members. A medical account may be established under IRC section 401(h) for the payment of medical benefits, and surplus qualified pension funds may be transferred to the 401(h) account under IRC section 420 to pay for qualified medical benefits.

Summary: The JCPP recommends that:

1. The Department of Retirement Systems with the assistance of the State Actuary proceed with application to the IRS for permission to make transfers under IRC 420;
2. the Legislature enact legislation to create a local government long term care risk pool and other administrative structures to distribute surplus funds for reimbursement of some local government LEOFF 1 retiree medical expenses;
3. a board be created to set policy for the risk pool;
4. all transfers under IRC 420 should be made in the state operating budget;
5. no transfers will be made without IRS permission; and
6. stop creation of additional disability boards.

These recommendations have no effect on the LEOFF 1 members or retirees medical benefits. There is also no effect on the current number or duties of the local disability boards or the responsibility of the local employer to pay for required medical benefits.

Recommendation:

Background:

The LEOFF 1 pension statute provides for pension, disability, survivor and medical benefits. The statute provides the funding for pension, disability and survivor benefits is the responsibility of the state with fixed contributions from local government employers and employees.

Local Disability board have the responsibility for determining the medical benefits an active or retired member is entitled to under the LEOFF 1 statute.

From the onset of LEOFF 1 in 1970, the responsibility for payment of the LEOFF 1 medical services benefit remained solely that of the LEOFF 1 employer abetted by self-insurance by the employer or the employer purchasing health insurance. To-date, this responsibility has not posed a problem. One of the major reasons for this is the LEOFF 1 membership is a relatively young system: the average retiree is age 62, while the average for all members is age 60. The incidence of higher medical costs tends to occur in older people. Obviously, the LEOFF 1 membership is going to age as time goes by; therefore, these costs are certain to increase in the future.

Pension benefits are usually actuarially pre-funded. This means that money is set aside in a pension fund to pay future benefits. Actuaries assume levels of investment return, future inflation, etc. to estimate how much needs to be set aside and invested to make these future benefit payments. When their estimates differ from experience, the plan may develop an unfunded liability or a surplus.

Medical benefits are not usually pre-funded. Most medical benefits are paid on a pay-as-you-go basis. No assumptions are made on long-term costs and no funds are invested. As retirees age, the cost of providing medical care rises. The risk of very high claims for any one employer is usually offset by purchasing medical insurance. Medical insurance is not a pre-funding plan. They serve only as a risk pool for all those who purchase insurance.

Medically necessary long term care costs are also required by LEOFF Plan 1. These costs differ from other medical costs in several respects:

1. Only a fraction of the total population will ever have long-term care costs. However, these costs can be very high when they do occur;
2. Long term care insurance is not a very well developed product. It is sold on an individual policy basis and only those healthy individuals are accepted. Those few local governments that have purchased LTC insurance have not been able to insure their older and less healthy retirees. It is also usually sold with substantial limitations on the amount and length of the benefit to be provided. Sold in this manner it is not a good fit for offsetting the risk of mandatory local government coverage.

The latest actuarial valuation of the LEOFF 1 medical benefits determined the present value of local government liabilities for retirees was at least $708 million. This assumes that all retirees will be covered by Medicare and that local government is not paying the Medicare Part B premium. The liability is well over $800 million when individual local government Medicare differences are included. This benefit is almost completely unfunded. Very few local governments have set aside funds to offset future cost.

The 1999 actuarial valuation of the LEOFF 1 pension benefits determined there is a $1.014 billion surplus. This surplus has developed primarily from extraordinary investment return over the last 15 years and relatively low inflation. As a result of the surplus, the legislature has stopped all employees, employer and state contributions to the pension fund.

This leaves the pension part of the system with a substantial surplus and the medical part with a substantial unfunded liability.

Proposal:

Apply to the IRS for permission to make transfers under IRC 420

IRC section 401(h) permits pension plans to provide for the payment of qualified medical expenses of retired employees if certain requirements are met. A set of qualification rules under IRC section 401(h) must include:

- A plan must specify the medical benefits available under the plan and must contain provisions for determining the amount that will be paid.
- Retiree medical benefits must be subordinate to the retirement benefits.

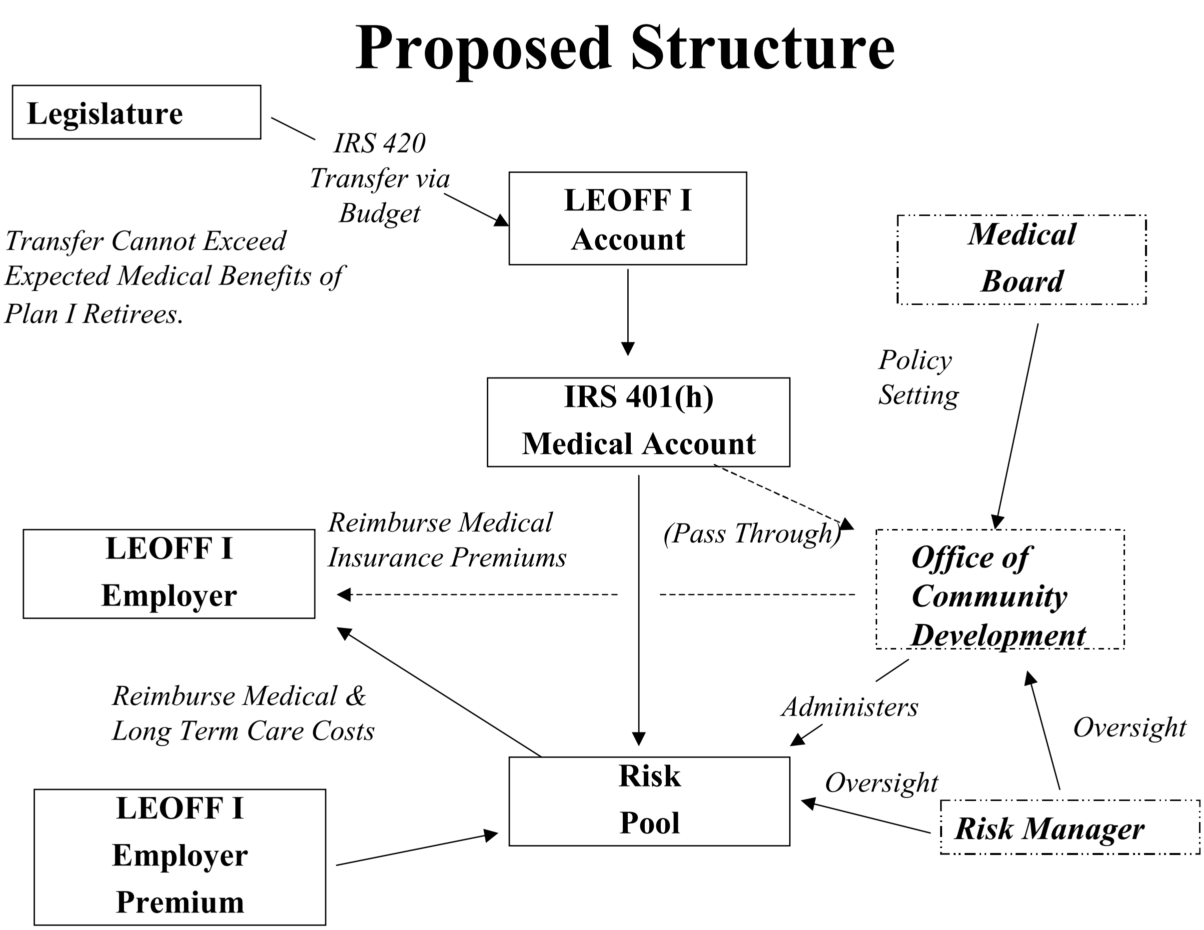
Federal law provides a method of funding an IRC Section 401(h) account based on transferring excess pension assets under IRC section 420. To make a qualified transfer under IRC section 420 several requirements must be observed, including:

- The corpus and income of money transferred may not be diverted for any use other than providing retiree medical benefits, including related necessary and appropriate administrative expenses.
- Only one transfer per year, and no transfers after December 31, 2005 unless the federal government again extends the expiration date of IRC section 420.
- Only excess pension assets may be transferred. For private sector plans the required funding for eligible excess is described in IRC section 420(e)(2), however the meaning of the subsection for governmental retirement plans is not clear. Part of the application process will be to determine the level of surplus assets required.
- Only the amount of the reasonably anticipated health care benefit costs for that year may be transferred.
- Transferred funds must be used only to pay qualified health benefits for LEOFF 1 retirees, for the year of the transfer, and unused amounts must be returned to the LEOFF 1 pension fund.

The application must be submitted to the IRS by the Plan Administrator-Department of Retirement Systems.

The Director must notify active LEOFF 1 employees of the application.

Create the Structure for Sharing Long Term Care Risks and an IRS 420 Transfer:



The structure necessary for utilizing the surplus assets includes the following:

Create a medical account:

Create a separate 401 (h) account within the LEOFF 1 pension fund for retiree medical benefits.

Establishing responsibility for the actuarial determinations:

The IRC allows for the transfer of retirement system assets to the 401(h) account when two tests are met: (1) the assets must be in excess of full funding; and (2) the amount transferred may not exceed the anticipated retiree medical costs for the particular year involved.

OSA will make three determinations known to the Office of Financial Management and the legislative fiscal committees. 1) the maximum amount of the excess assets (if any) that are available to the Legislature for transfer from the LEOFF 1 fund to the medical account based on the two tests stated earlier; 2) the maximum allowable transfer available to the Legislature from the medical account to the risk pool account; and 3) the allowable LEOFF 1 retiree medical cost reimbursement available to the Legislature for appropriation.

Authorize the transfers in the operating budget:

Enact statutory authorization for the appropriation act to make the necessary transfers from the LEOFF 1 pension funds to the LEOFF 1 medical account. This will happen only when all requirements are satisfied. The appropriations act will make four authorizations:

a. Transfer of funds from the LEOFF 1 pension fund to the LEOFF 1 Medical account;

b. Transfer from the medical account to the risk pool account. This transfer will augment the premiums to be required of LEOFF 1 employers to participate in the risk pool. These funds will be used solely for the reimbursement to the employers for LEOFF 1 retiree medical costs.

c. Authorize the Office of Community Development to reimburse LEOFF 1 employers LEOFF 1 medical costs. These funds would be to partially reimburse employer self-insurance or health insurance premiums on a per person basis (e.g., $100 per month per eligible LEOFF 1 retiree).

d. Authorize the use of the medical account for payment of administrative and actuarial expenses incurred by this program.

Create a local government long term care risk pool:

The purpose of the pool is to reimburse local government for long term care costs of LEOFF 1 retirees. Membership by local government in the pool would be optional. Reimbursement for expenses not normally covered by insurance plans may also be provided. Local government employers will pay premiums into the pool as needed. When possible, the operating budget will authorize the transfer of funds from the 401(h) account to the risk pool to supplement local government premiums.

The risk pool would be administered by the Department of Community and Economic Development. The decisions on benefits, membership, premiums, etc. would be determined by a board composed of representatives of local government and LEOFF 1 members. Oversight would be provided by the Risk Managers Office and actuarial assistance by the Office of State Actuary.

Following is a more detailed discussion of the risk pool.

LEOFF 1 Risk Pool:

Introduction:

A risk pool is simply an insurance mechanism for sharing a common risk or risks with other parties. In the instance of LEOFF 1, employers have a common risk: incurring long term care and major medical costs either partially covered by insurance or not covered by insurance at all. If a LEOFF 1 employer were to go it alone, incurring such cost could be crippling to the political subdivision. If, however, the LEOFF 1 employer joins with other LEOFF 1 employers in pooling financial resources, the cost impact would be far less.

Risk pools in no way reduce the cost of the benefit. It merely spreads the cost of benefits proportionately over all employers in the pool. A stable risk pool premium cannot be accomplished without substantial participation on the part of employers.

Risk pools do not usually accumulate sufficient assets to offset long term increasing costs. That is not their purpose. As the LEOFF 1 retiree population ages the cost of LTC will rise. This means the premiums paid into the risk pool will rise. The rise in risk pool premiums will likely be offset by a decrease in the total cost of LEOFF 1 retiree medical as their total number decreases.

Creation of the Board:

An executive board is established to set policy and premium rates for the operation of the proposed risk pool but not be involved in the day to day operation of the pool. It is recommended that this board consist of nine members appointed by the Governor. Under this proposal, the Governor would appoint the Chair with a term of four years.

The Chair is to be an individual not previously connected to LEOFF 1 either by employment or through service on a disability board. The individual, however, should be familiar with risk pool operation and medical and long term care matters.

The remaining eight members would consist of two members each from four groups: counties, cities and towns, fire protection districts and LEOFF employees. These eight would be selected by the Governor from recommendations made by their respective organizations.

For the first three groups, one of the appointed members must be an elected official. In the fourth group one appointed member must be a law enforcement officer and the other a fire fighter. One appointed member of the first three groups plus the law enforcement officer will have an initial term of office of two years and subsequent terms of office will be four years. The remaining members will have four year terms of office.

A Vice-Chair will be selected every two years and will act in the absence of the Chair. Vacancies on the board will be filled by the Governor from recommendations of the vacating member's organization and the selected person will serve for the remainder of the respective term of office. No compensation is to be received for service, only reimbursement for travel, lodging and sustenance related to board meetings.

It is suggested the Executive Board meet at least quarterly. The Executive Board is required to maintain minutes of their meetings and other records necessary for their operation. All of these records are to be public.

Duties of the Board:

The Executive Board will be the policy setting body for the risk pool program with rule making authority. But it is important to restate an earlier intention. Any medically necessary medical service must be as defined in LEOFF 1 statutes and approved by a disability board. The Board will only authorize reimbursement of certain medical costs incurred by LEOFF 1 employers providing these necessary and approved medical services. It cannot establish any new medical benefit. It will do the following in its policy direction of the risk pool.

Establish the Basis of Pool Membership: Through its rule making authority, the board will establish the conditions each employer must meet to participate in the risk pool. This will include such things as entering into an interlocal agreement with other LEOFF 1 employers; agreeing to payment of premiums; sharing in any losses; and how, if desired, an employer can withdraw from the risk pool. Although membership by local government is optional, it is unlikely an employer would be able to participate without including all of their LEOFF 1 retirees.

Define and Establish Pool Benefits: This risk pool, as other insurance plans, is not intended to pay all of the medical or long term costs incurred by the employer. The Board will determine to what degree, if any, the risk pool reimburses medical costs. The board may establish deductibles, co-pays, etc. as it feels best meets the needs of the employers. These deductibles and co-pays may be on an employer basis or on an individual retiree basis.

Authorize Fund Distribution from the Risk Pool: The Board will also determine the frequency, method and required information for the requesting and payment of reimbursements. These payments are anticipated as being authorized by the Board, and the Board notifying the Risk Pool Program to make the reimbursement.

Premiums: The Board, with the assistance of the actuary, must periodically determine the premium required of each participating employer of the pool. This premium will consist of two elements: funds sufficient to meet projected expenditures; and, funds necessary for the Office of Community Development to administer the risk pool. This will require participating members to periodically provide the Actuary's office with medical expenditure and other data sufficient to provide the projection of costs.

Non-Insured Major Medical Costs: The Board is authorized to provide reimbursement for major medical costs that are not usually covered by medical insurance policies, but are required by statute. It is left to the Board to determine what, if any, coverage will be included.

Reinsurance: The usual practice in insurance is to provide protection against losses above a certain level. This is done through reinsurance. The Board will determine the policy regarding purchasing of this coverage.

Office of Community Development:

The Office of Community Development (OCD), within the Department of Community, Trade and Economic Development, will operate the Risk Pool. OCD is currently responsible for a number of programs which deal with city and county law enforcement agencies. This means they already have established communications with LEOFF 1 employers. Moreover, OCD provides pass through funds from various state and federal government programs to local government. This means it is experienced in the transference of funds from the state level to local governments.

Duties: OCD will be required to either create a staff to operate and maintain the risk pool program, or engage a third party administrator to do so under OCD's direction. As previously noted, the operating funds for the risk pool would be derived a portion of the premium paid by the participating members. These funds, of course, would require regular appropriation.

Additionally, OCD would be required to distribute such monies from the medical account as directed by the Legislature for distribution to employers as direct reimbursement of insurance premiums or costs.

Office of Risk Management:

The Risk Manager, Office of Risk Management, Department of General Administration, is charged with the oversight of the management of risks which may bring about losses to state and local government assets and impact their revenues. It is given regulatory authority specifically for local government risk programs for property and liability or health and welfare plans.

Because the proposed risk pool program involves potential financial loss to its participating members, this program should come completely under the regulation of the Risk Manager. It is intended the proposed risk pool program comply in all respects to the oversight, reporting and other aspects of the rules and regulations of the Risk Manager.

The Risk Manager is to approve the proposed program prior to its establishment. This requires review of the program coverage, its financing, insurance or reinsurance needs, agreements entered into, etc. The Risk Manager is given up to 180 days to provide this approval.

Once a program is approved, it is subject to annual reporting requirements of the Risk Manager. This reporting includes disclosure of the insurance, actuarial, financial and management aspects of the program. The Risk Manager also performs periodic investigations of risk programs.

The Risk Manager also is a member of health and welfare advisory board along with the Insurance Commissioner and six other members. The other members are a representative of city management, a representative of county management, two representatives of local government self-insurance programs, and two representatives of local government employees. This advisory board assists the Risk Manager regarding creation and governance of programs and requiring annual reports. The proposed risk pool would be expected to comply with this advisory board and its rules.

Disability Boards:

This proposal makes no change to the current number or authority of the local disability boards. It also makes no change to the medical benefits required or the responsibility of the local government to pay for these benefits.

The only proposal involves the creation of new, additional boards. Each city with a population of less than 20,000 is currently serviced by its county disability board. When a county reaches a population of 20,000 it is required to create its own disability board. These cities are very likely to have more than a very few LEOFF 1 actives or retirees.

The proposal is to stop the creation of additional disability boards when cities reach 20,000 population.

LEOFF 1 Survivor Benefits for Post-retirement Marriage

Background:

LEOFF plan 1 survivor benefits present unique policy issues. The spousal benefit is automatic in nature, unlike the optional, actuarially-reduced benefits featured in most systems and plans. A spouse qualifies for a full continuation of the member's benefit if eligible, but eligibility requires marriage to the member for one year prior to separation from service (disability or retirement) and until the member's death. No survivor benefits exist for unqualified spouses of LEOFF plan 1 members.

Committee Activity:

Presentation:
September 20, 2000, Full Committee Meeting
Presentation:
October 18, 2000, Full Committee Meeting
Presentation:
November 15, 2000, Full Committee Meeting
Proposal Approved:
December 13, 2000, Full Committee Meeting

Recommendation to Legislature:

LEOFF plan 1 retirees who enter into a post-retirement marriage have the option of actuarially reducing their benefits and creating a survivor benefit for their post-retirement spouse. The option is limited to a one year window opening one year after the post-retirement marriage, and limited to members whose benefits are not subject to division from an earlier divorce.

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LEOFF 1 Survivor Benefits for Post-retirement Marriage

Joint Committee on Pension Policy

Revised January 3, 2001

Prepared by:

David Pringle
Research Analyst

Executive Summary

JCPP Recommendation:

An optional, actuarially reduced survivor benefit is added to LEOFF plan 1 for post-retirement spouses. Within a one-year window opening one year from the date of the post-retirement marriage, the member chooses to take an actuarial reduction to their benefit and designate their new spouse as their survivor beneficiary. The optional survivor benefit is limited to retirees whose benefits are not subject to a property settlement under a court decree of separation.

Actuarial reductions under such an approach would be approximately as shown on the table below.

Approximate Actuarial Reductions for a LEOFF Plan 1 Optional Survivor Benefit

Difference in age of survivor and member	Actuarial reduction, Joint & 100% Survivor Benefit	$1,000 Benefit is reduced to
5 years older than member	0.82	$820
No difference in age	0.77	$770
5 years younger than member	0.73	$730
10 years younger than member	0.69	$690
15 years younger than member	0.65	$650

I. Introduction

LEOFF plan 1 retirees who marry after they retire do not have survivor benefits available for their spouses. During the 2000 legislative session, legislation recommended by the Joint Committee on Pension Policy was enacted that provides an actuarially reduced survivor benefit to post-retirement marriage spouses for members of PERS, TRS, SERS, and LEOFF plan 2. This was limited to those members who did not designate a survivor at retirement, and those who did not have benefits subject to a property settlement under a court decree of separation.

II. Background

The Washington State retirement systems employ several distinct types of survivor benefits. One type is employed by the PERS, TRS, and SERS systems as well as LEOFF plan 2. They involve the choice at retirement to receive the benefit for the member's life alone, or to receive the equivalent value as an actuarially reduced benefit over the life of both the member and their designated survivor beneficiary.

LEOFF plan 1 has a different type of survivor benefit than most of the other plans. Rather than having a choice of survivor benefits, all members who have qualified survivors receive the survivor benefit, and it is paid for by all the contributions made to the system. Regardless of whether there is a qualified survivor the member does not have any reductions made to their benefit.

Table 1: Profile of LEOFF Plan 1 Membership - 1998-1999

Year	Total LEOFF 1	Active Members	Annuitants	Survivors (% of annuitants)
1998	9,667	1,968	6,420	1,014 (16%)
1999	9,604	1,743	6,553	1,070 (16%)

One point that makes analysis of the LEOFF plan 1 survivor population difficult is that there are no records kept in advance of the numbers of spouses that will qualify as survivors. When the member dies, a spouse is determined to qualify or not qualify for the benefit. This is unlike the PERS, TRS, or LEOFF plan 2 system in that the member must select their survivor beneficiary at retirement (or within the post-retirement marriage window after July 2001), and thus makes the existence of their survivor known in advance.

Qualified spousal survivors of retirees in LEOFF plan 1 are limited to those lawfully married to a member for one year prior to retirement or separation from service. If the member dies with qualifying children, then this may increase the amount of the survivor benefit payable to the surviving spouse, or the children may qualify for an independent survivor benefit if the member has no spouse.

Table 2: LEOFF Plan 1 Member Active and Retired Deaths - 1998-1999

Year	Active Member Deaths	Retired Member Deaths	Total Deaths	Died, no Survivor (% of total deaths)
1998	13	101	114	62 (54%)
1999	9	131	140	74 (53%)
1994-1999	70	614	684	unavailable

Table 2 demonstrates that over the past two years over 53% of LEOFF plan 1 members died without an eligible survivor.

III. Comparison to Washington State Patrol Retirement System

The Washington State Patrol Retirement System (WSPRS) is the only other system with an automatic survivor benefit for qualifying spouses like LEOFF plan 1, so comparison between the survivor benefits offered by each is common.

The WSPRS system allows post-retirement spouses who have been married to the retiree either before retirement until the members death, or for two years prior to the member's death. The spousal survivor benefit is the *lesser* of 50% of average final salary or the allowance paid to the member.

In comparison, the survivor benefit in LEOFF plan 1 is more limited in the qualification of spouses. The LEOFF Plan 1 survivor benefit is either 50% of the final average salary at the date of death if active, the amount of retirement allowance the vested member would have received at age 50, or the full continuation of the member's benefit if the member is retired or on disability leave.

Table 3: Profile of WSPRS Membership - 1998-1999

Year	Total WSPRS	Active Members	Annuitants	Survivors (% of Annuitants)
1998	1,738	929	582	98 (17%)
1999	1,722	968	604	110 (18%)

The total number of members and annuitants in the WSPRS is substantially less than in LEOFF plan 1, and the number who annually separate from the system is likewise smaller.

These figures might be compared to the LEOFF Plan 1 system presented in Table 1, but that comparison is misleading. The WSPRS is an open system, continuing to add active members.

The percentage of survivors in WSPRS would be larger if all entrants to WSPRS since the closure of LEOFF Plan 1 were removed. This is demonstrated in Table 4 for 1999.

Table 4: WSPRS Survivors as a Percent of Membership Excluding Entry Date after October 1, 1977

Year	Pre-1977 Total WSPRS	Pre-1977 Active Members	Pre-1977 Annuitants	Survivors (% of Annuitants)
1999	773	133	534	106 (20%)

Table 5: WSPRS Active and Retired Deaths and Survivors - 1998-1999

Year	Active Deaths	Retired Deaths	Total Deaths	Died, No Survivor (% of total deaths)
1998	0	4	4	1 (25%)
1999	1	12	13	4 (31%)
1994-1999	5	43	48	unavailable

While the numbers of member and annuitant deaths is small in any given year, over the past two years Table 5 suggests that the percentage of WSPRS members who died without an eligible survivor is somewhat less that in LEOFF plan 1, illustrated in Table 2. Comparison is difficult, however, as the population in WSPRS is small and difficult to generalize from, and may have unknown characteristics that increase or decrease the differences from LEOFF plan 1.

IV. **Analysis**

The average age of retirement for LEOFF plan 1 members was 53.26 years. According to the Washington Health Care Authority's study on the age of men when they marry, approximately 9.5 % of men marry at or after the age of 50. Of a total of 41,443 Washington marriages in 1998, 3,953 involved men over the age of

50.

Table 6: Marriages by Man's Age in Washington State - 1998

	<20	20-24	25-29	30-34	35-39	40-44	45-49	50-54	55-59	60-64	65+	Total
#	1,267	9,252	9,943	6,489	4,732	3,351	2,344	1,594	914	532	913	41,443
%	3%	22%	24%	16%	11%	8%	6%	4%	2%	1%	2%	100%

Table 7: LEOFF Plan 1 Retirements and Disabilities by Age - 1994-1999

Age	Service Retirement	Disability Retirement	Total
<34	-	6	6
35-39	-	62	62
40-44	-	221	221
45-49	-	417	417
50-54	353	308	661
55-59	123	73	196
60+	53	14	67
Total	**529**	**1,101**	**1,630**

A significant portion of LEOFF plan 1 members separated from service because of disability before reaching the retirement age of 50. Table 7 demonstrates this during the 1994-1999 period, where 706 of the total 1,630 separations from service, 43.3%, were by disability retirement prior to age 50. This is important because spouses who marry members less than one year before the disability retirement are also ineligible for the LEOFF plan 1 survivor benefit. An exception to the one year requirement exists for members who die in the line of duty.

Figure 1: Age of LEOFF Plan 1 Spousal Survivors - 1999

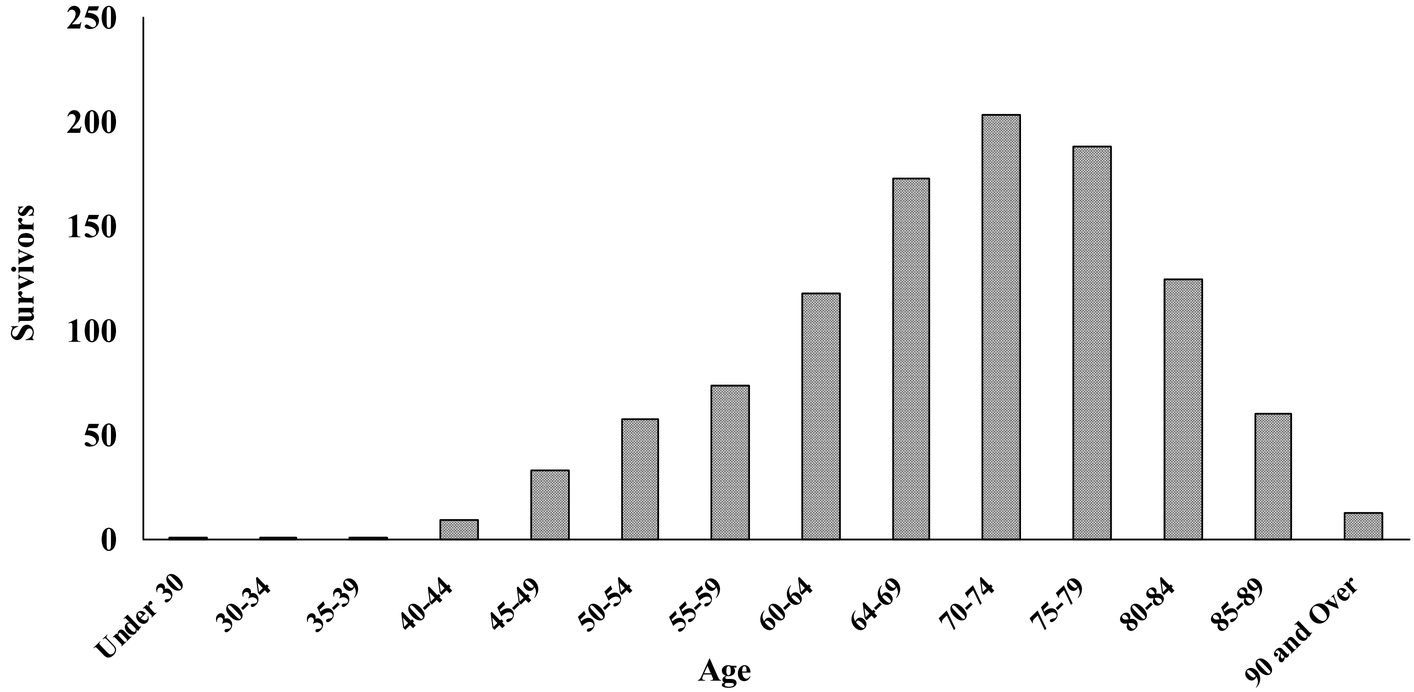
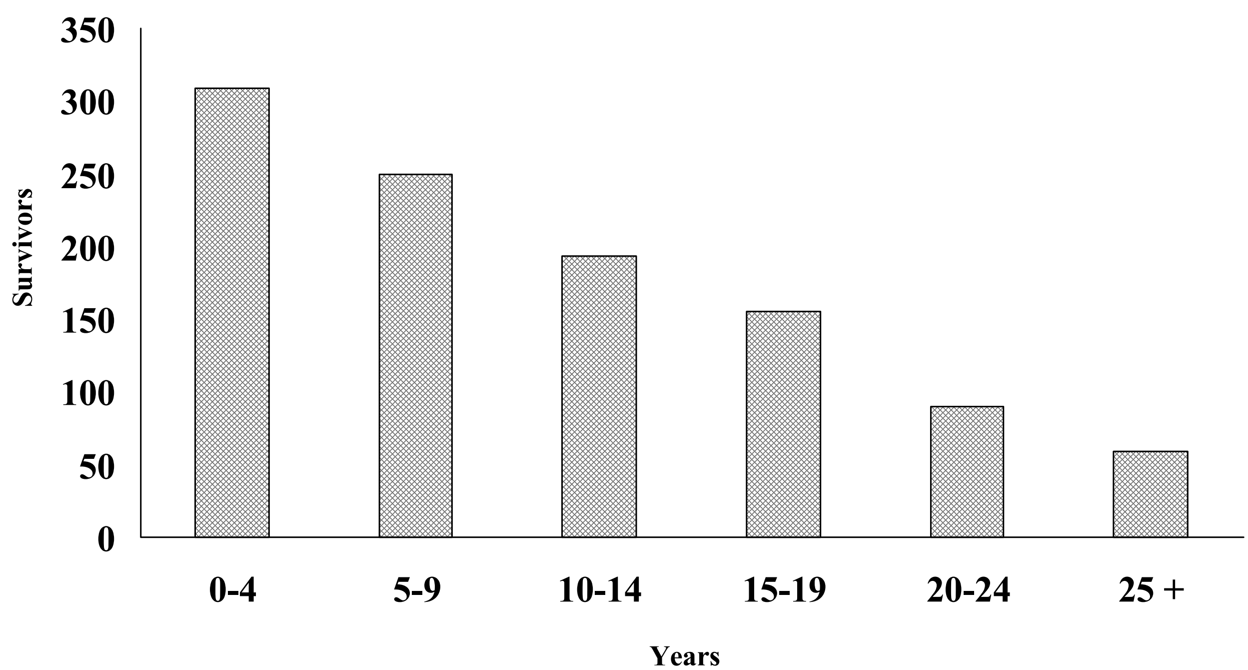


Figure 2: LEOFF Plan 1, Years Spousal Survivors Have received benefits



Figures 1 and 2 illustrate the makeup of the LEOFF plan 1 spousal survivor beneficiaries. As expected most are older, clustered in the 65-80 year age groups, with significant numbers under age 60 and twelve at less than 45 years of age. The distribution of spousal survivors by the years of benefit receipt follows, showing more receive the survivor benefit for fewer years but that a significant number of survivors receive benefits for more than 20 years.

V. Possible Approaches

1. Optional, actuarially reduced survivor benefit for ineligible spouses.

An optional, actuarially reduced survivor benefit could be added to LEOFF plan 1 for post-retirement spouses. Within a one-year window opening one year from the date of the post-retirement marriage, the member could take an actuarial reduction to their benefit and designate their new spouse as their survivor beneficiary. The optional survivor benefit would be limited to retirees whose benefits are not subject to a property settlement under a court decree of separation.

The actuarial reductions under such an approach would be approximately as shown on Table 8.

Table 8: Actuarial reductions for a LEOFF plan 1 optional survivor benefit.

Difference in age of survivor and member	Actuarial reduction, Joint & 100% Survivor Benefit
5 years older than member	0.82
No difference in age	0.77
5 years younger than member	0.73
10 years younger than member	0.69
15 years younger than member	0.65

2. **Remove the eligibility requirements for spousal survivors.**

The requirement that a spouse be married to a member for one year prior to separation from service could be removed. This would add additional beneficiaries and costs to the system by providing a full continuation of members' benefits to individuals who would not receive LEOFF plan 1 benefits under current law.

During the 1999 legislative session, Senate Bill 5727 proposed removal of the spousal survivor eligibility requirements. The 1999 proposal would have also continued eligibility for the survivor benefit to ex-spouses of retirees who were awarded survivor benefits in a court order pursuant to the divorce.

It is difficult to accurately assess how many members of LEOFF Plan 1 have survivors if the spousal eligibility requirements are removed. If all LEOFF Plan 1 members left a surviving spouse the actuarial impact of removing the one-year prior to separation from service requirement would be an approximate $450 million increase in the Present Value of Fully Projected Benefits. The actual amount would be less, as not all members would die with a spouse.

VI. **JCPP Recommendation:**

An optional, actuarially reduced survivor benefit is added to LEOFF plan 1 for post-retirement spouses. Within a one-year window opening one year from the date of the post-retirement marriage, the member chooses to take an actuarial reduction to their benefit and designate their new spouse as their survivor beneficiary. The optional survivor benefit is limited to retirees whose benefits are not subject to a property settlement under a court decree of separation.

Actuarial reductions under such an approach would be approximately as shown on the table below.

Approximate Actuarial Reductions for a LEOFF Plan 1 Optional Survivor Benefit

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Appendix

Table 2: LEOFF 1 Survivors current age, and years that survivor has received benefit

	Years survivor has received benefit																															Total
	0	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17	18	19	20	21	22	23	24	25	26	27	28	29	30	
Survivor current age																																
UNDER 30	0	0	0	0	0	0	0	0	0	0	0	1	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	1
30-<35	0	0	0	0	1	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	1
35-<40	1	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	1
40-<45	1	2	0	0	1	1	1	0	0	0	0	0	0	1	0	0	0	0	0	0	0	0	1	1	0	0	0	0	0	0	0	9
45-<50	0	4	3	4	3	2	1	0	0	1	0	1	3	2	0	0	1	3	1	0	2	1	1	0	0	0	0	0	0	0	0	33
50-<55	0	4	5	4	1	2	4	3	1	2	5	2	2	1	3	4	1	1	2	1	3	3	0	2	0	1	0	0	0	1	0	58
55-<60	2	8	4	7	4	3	10	5	3	2	1	2	2	3	2	3	3	1	1	1	1	2	0	0	1	0	1	0	1	1	0	74
60-<65	7	13	7	10	13	1	8	4	6	5	4	2	2	3	3	3	2	0	4	2	2	0	2	3	3	3	1	1	2	2	0	118
65-<70	10	14	11	6	7	9	9	8	7	6	9	7	8	7	5	4	4	8	10	3	1	2	2	4	2	2	2	0	1	3	2	173
70-<75	5	8	9	13	16	14	11	12	11	11	13	8	8	7	6	7	3	4	2	7	3	4	6	7	2	4	1	1	0	0	0	203
75-<80	12	11	8	11	12	9	5	12	4	6	13	6	5	11	7	6	8	4	3	8	0	4	4	6	2	3	3	4	0	1	0	188
80-<85	4	9	4	8	10	9	4	9	5	3	3	2	6	2	2	11	4	5	3	5	2	2	1	0	1	0	6	1	0	3	1	125
85-<90	0	2	3	1	4	2	4	3	4	3	2	2	3	1	2	3	3	1	2	1	1	1	1	2	2	2	0	2	2	1	0	60
90 AND OVER	0	0	0	1	1	1	1	2	0	1	0	3	0	0	1	0	1	0	0	1	0	0	0	0	0	0	0	0	0	0	0	13
Total	42	75	54	65	73	53	58	58	41	40	50	36	39	38	31	41	30	27	28	29	15	19	18	25	13	15	14	9	6	12	3	1057

NOTE: *The years survivor has received benefit is rounded to the nearest year.*
NOTE: *This data excludes child survivor beneficiaries.*

FISCAL NOTE

REQUEST NO.

RESPONDING AGENCY:	CODE:	DATE:	BILL NUMBER:
Office of the State Actuary	**035**	**10/31/00**	**Z-0241.2/01 2nd Draft**

SUMMARY:

This bill impacts the Law Enforcement Officers' and Fire Fighters' Retirement System (LEOFF) Plan 1 by allowing the member to elect an actuarially reduced benefit which provides that a portion of their pension will continue for the life of their post-retirement spouse.

This election must be made during the second year of the post retirement marriage, or within one year of the adoption of the rules providing for this election, if later.

To qualify for the election, the retirement allowance and/or subsequent death benefit must not be payable to an ex-spouse.

Effective Date: No later than July 1, 2002

BACKGROUND DISCUSSION:

Spouses who are married to a member for one year prior to retirement or separation from service (and are still married at the member's death) currently receive a death benefit without a reduction in their pension.

MEMBERS IMPACTED:

During 1999 DRS reported 129 deaths among disabled and retired members. Forty-nine, or over 35%, did not receive a survivor benefit. We do not have any information on how many of these had a post-retirement spouse and might have made this election.

We estimate that for a typical member who elects a 100% Joint and Survivor, the reduced benefit would be between 70 to 75 percent, assuming a spouse five years younger to the same age as the member. Actual reduction factors have not been calculated. There are currently 6,553 retirees and disabled retirees with an average yearly benefit of \$29,444. Thus the typical member who makes this election would have their benefit reduced from \$29,444 to something between \$20,611 and \$22,083. There are 1,743 active members who after they retire may make this election as well.

FISCAL IMPACT:

Actuarial Determinations:

Since these benefits are provided by an actuarial reduction there is no fiscal impact on the system.

Gerald B. Allard, State Actuary

LEOFF 1 Survivor Benefits for Pre-retirement Divorce

Background:

LEOFF plan 1 retirement benefit payments may be divided by a court between a member and divorcing spouse prior to retirement. For example, a court could specify that half of each retirement benefit payment be made to each of the divorcing member and spouse. When the member dies, all payments cease. There is no survivor benefit in LEOFF plan 1 that a court can award to a divorcing spouse of a member. For additional background on LEOFF plan 1 survivor benefits, see the section in this report on "LEOFF plan 1 Survivor Benefits for Post-retirement Marriage."

Committee Activity:

Presentation - Proposal Approved:
December 13, 2000, Full Committee Meeting

Recommendation to Legislature:

For divorces involving active LEOFF plan 1 members after July 1, 2002, a judge may specify that the portion of a member's benefit that is awarded to the ex-spouse be payed for the life of the ex-spouse, rather than just the life of the member.

Staff Contact:

David Pringle – 586-7616 – pringle_da@leg.wa.gov

LEOFF 1 Survivor Benefits for Pre-retirement Divorce

Bill Summary

Permitting continuation of divided LEOFF plan 1 benefits to ex-spouses in pre-retirement divorce orders made after July 1, 2002.

Currently, the divorcing spouse of an active LEOFF plan 1 member may be awarded a split benefit in a divorce proceeding, but this portion of the member's benefit will cease when the member dies. Unlike other systems or plans such as PERS or LEOFF plan 2, no survivor benefit is available for pre-retirement selection via court order.

In the event of a pre-retirement divorce after July 1, 2002, a court ordered split of a LEOFF plan 1 member's retirement benefit payment may specify that the portion of the benefit payed to the ex-spouse will continue for the life of the ex-spouse.

FISCAL NOTE

REQUEST NO.

RESPONDING AGENCY:	CODE:	DATE:	BILL NUMBER:
Office of the State Actuary	**035**	**01/04/01**	**Z-0336.1/01**

SUMMARY:

This bill impacts the Law Enforcement Officers' and Fire Fighters' Retirement System (LEOFF) Plan 1 by allowing the benefit payable to an ex-spouse to continue after the death of the member if provided for in a court order or court-approved property settlement. This provision applies only to divorces after July 1, 2002 and before the member separates from service.

Effective Date: July 1, 2002

BACKGROUND DISCUSSION:

Currently the court can divide the portion of member's pension payable while the member is alive. Without this change the court can not order the plan to provide a benefit which is not already provided by the plan. And thus can not order the plan to continue the benefit after the death of the member. This bill would allow the benefit to be split without any reduction to the total benefits paid due to the longer life expectancy of the ex-spouse.

A similar problem exists with the Washington State Patrol Retirement System (WSP) which also provides a death benefit at no cost to the member. This is not a problem of the other plans of the state where the death benefit is provided by a joint and survivor option which is paid for by the member through a reduction in the benefit. In this case the court can direct the participant to select a reduced joint and survivor option with the ex-spouse as the beneficiary. If the ex-spouse should die first the full pension reverts to the member.

The death benefits to a spouse (due to re-marriage) are not affected by this provision.

MEMBERS IMPACTED:

Any of the 1,743 active members of this system could be affected by this bill if they should divorce after July 1, 2002 and before they separate from service.

This would mean that a portion of the member's benefit (paid to the ex-spouse) would be payable over the life of the ex-spouse instead of the member (or the member and ex-spouse as with current court orders).

Since spouses of male members are on average 2 to 3 years younger than the member, and females tend to live longer than males this would mean this benefit would continue for a longer period of time. The reverse would be true for spouses of female members but most retirees from LEOFF 1 are male. The table below shows the life expectancy for males and females at various ages :

Age	Male Life Expectancy	Female Life Expectancy
55	24	30
50	29	35
45	33	40
40	38	44
35	43	49
30	48	54

We do not have any information of the number of divorces among the LEOFF members, the percentage of court orders awarded or the portion of the benefit awarded by court order.

FISCAL IMPACT:

Since we do not have essential information needed to determine the cost of this provision we can only illustrate what the range of costs might be using various ranges of assumptions as to what percentage of the members divorce each year, and what percentage of their benefit might be divided by a court order, if any.

The national divorce rate is 2% a year. The rate is lower for older people with spouses about the same age. The rate is quite a bit higher for older people with a spouse who is much younger. In the state of Washington the divorce rate is 5% a year.

There are currently 145 divided benefits (per DRS) payable out of 6,553 retirees and disabled participants in LEOFF 1. This might increase if a better death benefit is provided from the plan.

Actuarial Determinations:

Just to illustrate what the costs might be we have calculated the costs assuming:

The bill will impact the actuarial funding of the system by increasing the present value of benefits payable under the Law Enforcement Officers' and Fire Fighters' Retirement System (plan 1) and the required actuarial contribution rate as shown below:

1. 2% of the members divorce once, with 50% of the benefit paid to the ex-spouse.

Law Enforcement Officers' and Fire Fighters' Retirement System (plan 1)

(Dollars in Millions)	**Current**	**Increase**	**Total**
Actuarial Present Value of Projected Benefits The Value of the Total Commitment to all Current Members	$4,262	$3	$4,265
Unfunded Actuarial Accrued Liability The Portion of the Plan 1 Liability that is Amortized until 2024	$(894)	$3	$(891)
Unfunded Liability (PBO) The Value of the Total Commitment to all Current Members Attributable to Past Service	$(1,014)	$2	$(1,012)
Required Contribution Rate	0%	.57%	0%

The increase in the contribution rate is calculated as being paid from increases in the normal cost payable over plan 1 members salaries only, rather than an amortization of an unfunded liability payable until 2024.

or

2. 20% of the members divorce once, with 50% of the benefit paid to the ex-spouse.

(Dollars in Millions)	**Current**	**Increase**	**Total**
Actuarial Present Value of Projected Benefits The Value of the Total Commitment to all Current Members	$4,262	$26	$4,288
Unfunded Actuarial Accrued Liability The Portion of the Plan 1 Liability that is Amortized until 2024	$(894)	$26	$(868)
Unfunded Liability (PBO) The Value of the Total Commitment to all Current Members Attributable to Past Service	$(1,014)	$22	$(992)
Required Contribution Rate	0%	5.69%	0%

The increase in the contribution rate is calculated as being paid from increases in the normal cost payable over plan 1 members salaries only, rather than an amortization of an unfunded liability payable until 2024.

Fiscal Budget Determinations:

Because the plan remains in surplus their would be no fiscal impact.

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Gerald B. Allard, State Actuary

LEOFF 2 Disability Age Corrections

Background:

The 2000 Legislature changed the regular retirement age for Law Enforcement Officers' and Fire Fighters' Retirement System, plan 2 members from age 55 to age 53. The age from which actuarial reductions are made for disability retirements remained at 55.

Committee Activity:

Presentation: LEOFF Disability Age Technical Corrections
November 15, 2000, Full Committee Meeting
Proposal Approved:
December 13, 2000, Full Committee Meeting

Recommendation to Legislature:

The age from which LEOFF plan 2 disability allowances are actuarially reduced is changed from 55 to 53.

Staff Contact:

David Pringle – 586-7616 – pringle_da@leg.wa.gov

LEOFF Plan 2 Disability Age
Bill Summary

This proposal changes the age from which the disability allowance is actuarially reduced from 55 years to 53, matching the reduction in the normal LEOFF plan 2 retirement age adopted by the 2000 Legislature.

Among the provisions of the bill enacted by the 2000 Legislature ESSB 6530, the PERS 2/3 bill, was an improvement in the early retirement reduction factors(ERRF) for PERS, TRS, SERS, and LEOFF plan 2. For LEOFF plan 2, the normal retirement age was also reduced from age 55 to age 53. Concerns about the effect of reducing the ERRF on disability retirements caused disability provisions to be removed from the legislative proposals, inadvertently resulting in a different base age being adopted for the calculation of early retirements and disability retirements.

FISCAL NOTE

REQUEST NO.

RESPONDING AGENCY:	CODE:	DATE:	BILL NUMBER:
Office of the State Actuary	**035**	**01/04/01**	**Z-0266.2/01**

SUMMARY:

This bill impacts the Law Enforcement Officers' and Fire Fighters' Retirement System(LEOFF) Plan 2 by changing the age from which the early reduction starts for disability from age 55 to 53.

Effective Date: 90 Days After Session Ends

BACKGROUND DISCUSSION:

The reduction for early commencement in retirement and death benefits starts at age 53.

MEMBERS IMPACTED:

Any of the 12,713 active members of this system could be affected by this bill if they should become disabled before being eligible for early retirement.

We estimate that for a typical member impacted by this bill, the increase in benefits would be about a 22% increase in their disability benefit, assuming the member does not elect to withdraw their accumulated contributions. Since the accumulated contributions might be worth more, particularly at the younger ages many members might elect to withdrawal these amounts and this bill would provide no increase.

FISCAL IMPACT:

Actuarial Determinations:

The bill will impact the actuarial funding of the system by increasing the present value of benefits payable under the System and the required actuarial contribution rate as shown below:

System:

(Dollars in Millions)	**Current**	**Increase**	**Total**
Actuarial Present Value of Projected Benefits The Value of the Total Commitment to all Current Members	$3,110	$2.5	$3,113
Unfunded Actuarial Accrued Liability The Portion of the Plan 1 Liability that is Amortized until 2024	N/A	N/A	N/A
Unfunded Liability (PBO) The Value of the Total Commitment to all Current Members Attributable to Past Service	$1,408	$1.3	$1,409
Required Contribution Rate	11.54%	0.02%	11.56%

Fiscal Budget Determinations:

As a result of the higher required contribution rate, the increase in funding expenditures is projected to be:

Increase in Contribution Rates:	
Employee	0.01%
Employer	0.01%
State	0.00%
Costs (in Millions):	
2001-2003	
State:	
General Fund	$0.00
Non-General Fund	0.00
Total State	**$0.00**
Local Government	$0.20
2001-2005	
State:	
General Fund	$0.00
Non-General Fund	0.00
Total State	**$0.00**
Local Government	$0.40

2001-2026	
State:	
General Fund	$0.00
Non-General Fund	0.00
Total State	**$0.00**
Local Government	$4.50

State Actuary's Comments:

Gerald B. Allard, State Actuary

Optional Plan 2 or 3 for TRS and SERS

Background:

The 2000 Legislature directed the JCPP to study providing an option of Plan 2 or Plan 3 for new employees to the School Employees' Retirement System (SERS) and the Teachers' Retirement System (TRS). Following the creation of TRS Plan 3 on July 1, 1996 and SERS Plan 3 on September 1, 2000, all new members of both plans enter Plan 3.

Committee Activity:

Roundtable:
October 18, 2000, Full Committee Meeting
Presentation:
November 15, 2000, Full Committee Meeting
Presentation: Proposal, Proposal not approved
December 13, 2000, Full Committee Meeting

Recommendation to Legislature:

That the proposal to create an optional plan 2 or plan 3 for new employees not be recommended to the Legislature.

Staff Contact:

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Optional Plan 2 or 3 for TRS and SERS

Joint Committee on Pension Policy

Revised January 4, 2001

Prepared by:

David Pringle
Research Analyst

I. Background

A. Description of the Problem/Situation:

Chapter 230, Laws of 2000: *"The joint committee on pension policy shall study the feasibility of providing an option of plan 2 or plan 3 for school employees' retirement systems and teachers' retirement systems new employees, and it shall provide recommendations to the appropriate legislative committees by January 1, 2001."*

B. General Information:

1. Introduction

Three of the systems in the Washington State Retirement Systems provide for a plan 3 "hybrid"defined benefit/defined contribution retirement plan. The first, Teachers' Retirement System (TRS), plan 3, began plan 3 membership during 1996. The second, the School Employee's Retirement System (SERS), plan 3, was created along with the division of the SERS membership from the Public Employees' Retirement System (PERS) on September 1, 2000.

The third, PERS plan 3, was adopted by the 2000 legislature and unlike the previous plan 3's, is offered as a choice alongside plan 2 for new entrants to the PERS system.

2. The Plan 2 and Plan 3 Designs

Plan 2 is a defined benefit design offering members a formula of 2 percent of their final average salary for each year of credited service. Members and employers contribute equally to the funding of the benefit, and contribution rates for both change equally with the funding requirements and any increase in benefits.

Plan 3 in contrast is a hybrid defined benefit-defined contribution design. Employer contributions fund a defined benefit amounting to 1 percent of a member's final average salary for each year of credited service. Member contributions are made according to an irrevocably selected plan selected by the member within 90 days of becoming a member of plan 3. The lowest available rate is 5 percent of member pay.

Member contributions fund a defined contribution individual member account. The member can invest the contributions that accumulate in their member accounts in a variety of different options that suit their individual preferences and needs.

3. *Plan Membership in TRS, SERS and PERS*

a. ***TRS 3***

The Teachers' Retirement System, plan 3 was created on July 1, 1996, and all new members to the TRS system after that date became members of plan 3. Existing plan 2 members were given the choice to irrevocably transfer to plan 3.

Table #1

TRS Plan 2 and Plan 3 Membership, 1998-1999

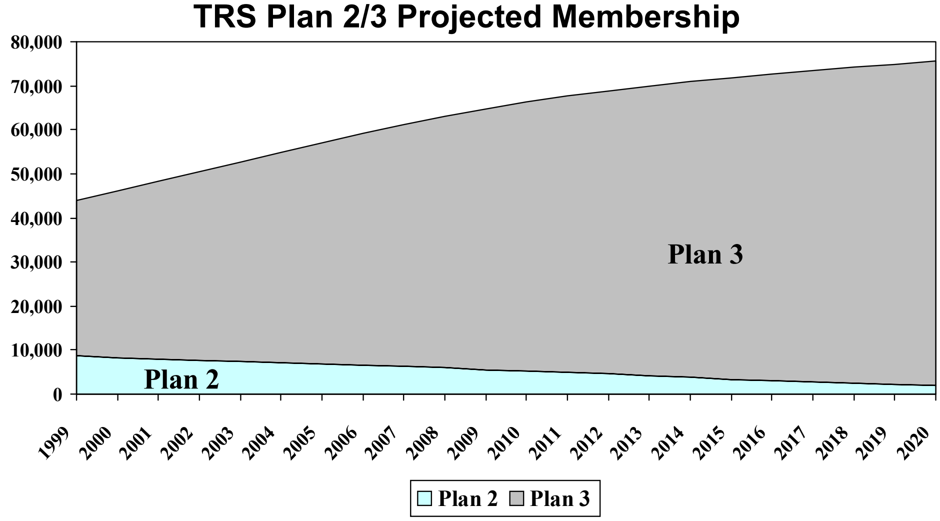
	Plan 2			Plan 3		
	Active	**Retired**	**Disabled**	**Active**	**Retired**	**Disabled**
1998	9,058	265	0	32,605	25,595	822
1999	8,663	347	0	35,284	40	0

Upon the creation of TRS plan 3 , the majority of the TRS plan 2 membership chose membership in plan 3. Table 1 demonstrates this by showing the population in each of the TRS plans for the past two years.

There are about 4,000 new members to TRS plan 3 each year, as shown in Table 6 below. As most of the TRS plan 2 membership transferred to TRS plan 3 and there are no new TRS plan 2 members, the remaining TRS plan 2 membership represents a small and declining portion of the total population of the two plans. This decline is projected to be from about 8,700 plan 2 members in 1999 to about 1,900 in 2020.

Table #2

TRS Plan 2/3 Projected Membership



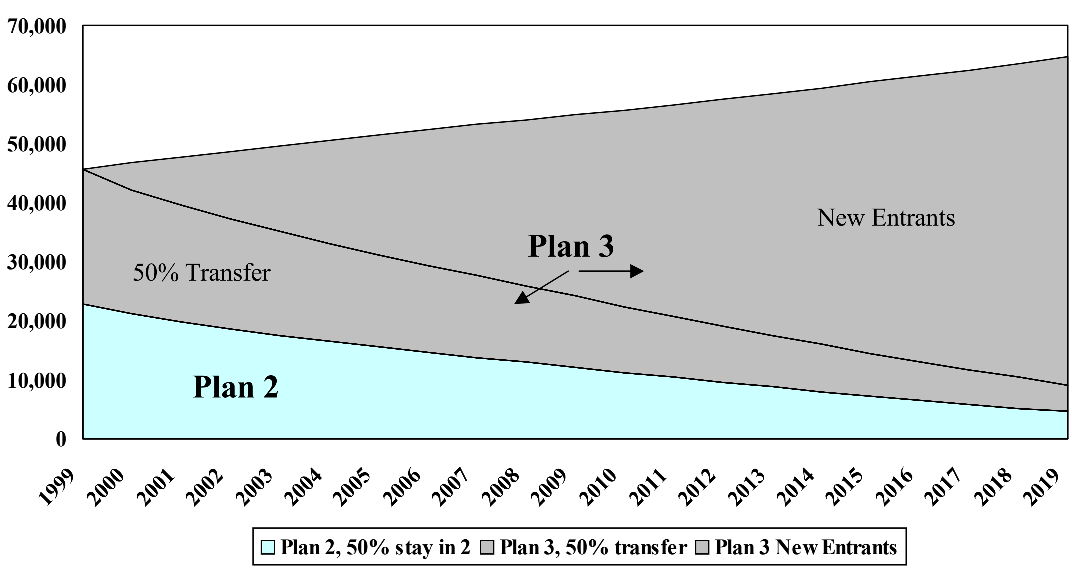
b. ***SERS 3***

The School Employees system, including plans 2 and 3, came into effect on September 1, 2000. Members joining the system after this date enter plan 3.

"Existing members," those who were members of PERS plan 2 became members of SERS plan 2 with an irrevocable choice to transfer to SERS plan 3. Members of SERS plan 2 may transfer during the transfer window, which extends from September 1, 2000 to February 28, 2001. Those members choosing to transfer during the window are eligible for an additional transfer payment of 130 percent of their member account balances. SERS plan 2 members may transfer to plan 3 after the transfer window during the month of January, but do not receive the additional payment.

As the transfer window for SERS plan 2 members will remain open until February of 2001, the rate of transfer to plan 3 is still unknown. This makes projections of future membership in SERS plans 2 and 3, more speculative than TRS. The Projected SERS Membership graph illustrates a projection of the future membership if 50% of the SERS plan 2 membership chooses to transfer to plan 3.

Table #3
SERS Plan 2/3 Projected Membership

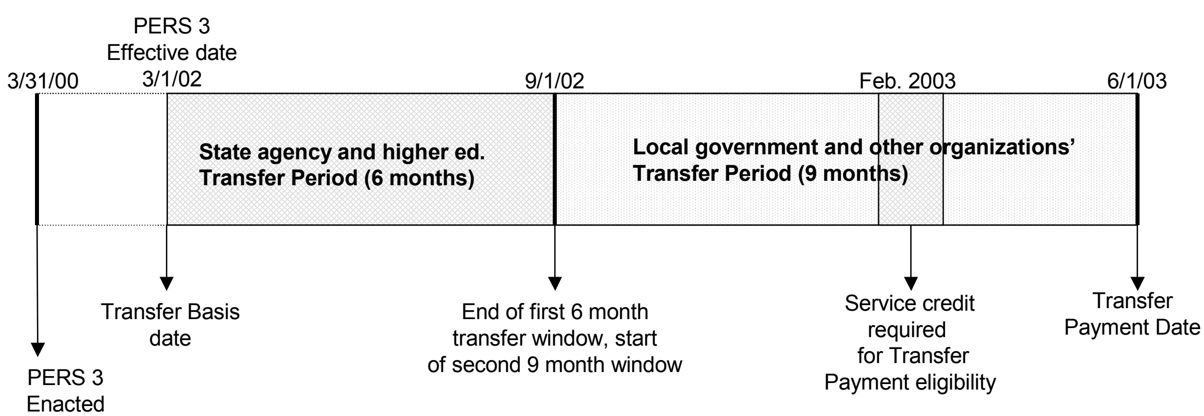


The total SERS membership in 1999 totaled about 46,000. On Table 3 “SERS Plan 3 Projected Membership”, half of the current members begin in each of plan 2 and plan 3. About 5,500 members join SERS each year (see Table 6 below), and all of these enter plan 3. In this scenario, the plan 2 membership starts at about 23,000 and declines to about 4,000 by 2020. While the number of members that transferred from plan 2 to plan 3 declines similarly, all new members boost the total plan 3 membership from about 23,000 in 1999 to nearly 62,000 by 2020.

c. ***Optional PERS 2/3***

The Public Employees Retirement System optional Plan 3 was created during the 2000 legislative session and will come into effect on March 1, 2002. New members to PERS will have a one-time irrevocable choice to enter plan 2 or plan 3. This choice between plan 2 and plan 3 is the “optional” feature commonly referred to. The PERS 3 Timeline below illustrates the period over which PERS plan 2/3 will come into effect.

Table #4
PERS 3 Timeline



Transfer Basis Date - Member account balance on 3/1/02 is the basis for the Transfer Payment.
Transfer Payment - Member account balance is increased by 110% for state agency members or 111% for local government and other members.

Each new PERS member will have a 90-day period during which they may irrevocably choose to enter plan 2, choose to enter plan 3 at one of the various member contribution rate schedules provided in chapter 41.34 RCW, or to be placed by default into plan 3 at the minimum member contribution rate. Member contributions during the option period are at the plan 2 rate.

Current PERS Plan 2 members will have the option to transfer to plan 3 – similar to the transfer option that has been offered to TRS and SERS plan 2 members. Two transfer windows are created for state and local PERS 2 members, beginning in March 2002 and September 2002 respectively.

Members who transfer from plan 2 to plan 3 during their designated window will receive a 110% or 111% transfer payment. PERS 2 members who do not choose to transfer to plan 3 during their transfer window may move to plan 3 in January of subsequent years, but do not receive the transfer payments.

The two transfer window approach was used for the first time in PERS because of concerns about the administrative complexity of the optional plan 2/3 approach, and the challenge of implementing the plan over the diverse and numerous PERS employer and employee populations.

Members are prohibited from transferring from plan 2 to plan 3 if they previously retired from plan 2, and in order to be eligible for the transfer payment they also must have a balance in their member accounts at the "transfer basis date" (See Figure 3), they must be active during the month of February 2003, and unless they are deceased they must have an individual member account on the transfer payment date, June 1, 2003.

C. Significance of the Issue to Policy:

Adopting optional plans 2/3 is a policy of great significance to the future makeup of Washington's retirement systems. Plan 3 was developed as a replacement for plan 2. Current employees were offered a transfer and new employees were mandated into plan 3. The TRS plan 2/3 projected membership graph on page 2 demonstrates that where this occurs, it takes only a few years for the vast majority of employees to be covered by one plan design. Plan 2 membership clearly will decline over time as members terminate employment or retire.

Providing new members with the option of plan 2 or 3 will maintain the viability of the plan 2 design indefinitely. Table 5 demonstrates that it is likely there will be a significant number of employees in both plans in the future if the option of plan 2 or 3 is in place.

Work on the pension systems will now have to be directed towards finding solutions to problems that work not just in one plan design but in both designs. The significant differences between the two designs may make this very challenging. Benefit increases will necessarily be oriented towards the defined benefit features shared by both plans 2 and 3.

Optional plans for new hires will add a dynamic to the systems that Washington has never experienced. Some of the challenges that may be raised by the optional design include:

- Employees in identical positions (for example age, service period, and pay) will both be able to compare their benefits between plans 2 and 3, and at different points in time see that one plan offers advantages over the other.

- Employees will expect that improvements to one plan will have a corresponding improvement to the other. Changes to each plan will change the basis upon which the members made their irrevocable choice of plans.

- An employee cannot know their future with certainty, making the choice of the better plan similarly uncertain.

A major policy the state has followed from the mid 1970s has been to have all public employees in plans with similar plan designs. This policy manifested itself in the similarity of the plan 2 designs and again in the plan 3 designs. This policy has not been carried out completely. LEOFF plan 2 is significantly different from the other plan 2s and the PERS optional plan 2 or 3 is different from SERS and TRS. Clearly, there are substantial policy choices to be made in regard to the future of these plans.

II. Policy Analysis

A. Question 1 - What is the feasibility of providing TRS and SERS with an optional plan 2/3 similar to the PERS 2/3 plan passed by the 2000 legislature?

Question 2 - What is the feasibility of providing TRS and SERS with an optional plan 2/3 that also allows members who entered plan 3 without the choice of plan 2 the ability to transfer to plan 2?

B. Analytic Approach:

1. Optional Plan 2/3 Designs

This discussion easily divides into two areas: 1) New hires after some future effective date; and 2) those who were hired after the effective date of plan 3 and were mandated into plan 3.

a. ***New Hires***

Many of the issues related to providing an option for future hires of SERS and TRS are administrative. The department of retirement systems is preparing to implement the option for PERS new hires after March 1, 2002. Allowing members the option also entails providing the member sufficient educational information to make an informed choice. A process was developed to educate members for the purpose of deciding whether or not to transfer from plan 2 to plan 3. The educational material needed and the processes are different for informing new hires.

The significant workload in the DRS for implementing PERS Plan 3 will delay the implementation of SERS and TRS optional Plan 2 or 3 until after the PERS 3 transfer period is closed. That would put the earliest implementation date at approximately June of 2003.

b. ***Those Mandated into Plan 3***

Those employees first hired after the effective dates of plan 3 of SERS and TRS were mandated into plan 3. They have not had the choice of plan 2 or 3. This would be all SERS members hired after August 30, 2000 and all TRS members hired after June 30, 1996.

2. A Future Hires-only Approach for a Plan 2/3 in TRS and SERS

This approach offers the choice of plan 2 or plan 3 membership only to those members who first become members after the creation of the optional plan 2/3.

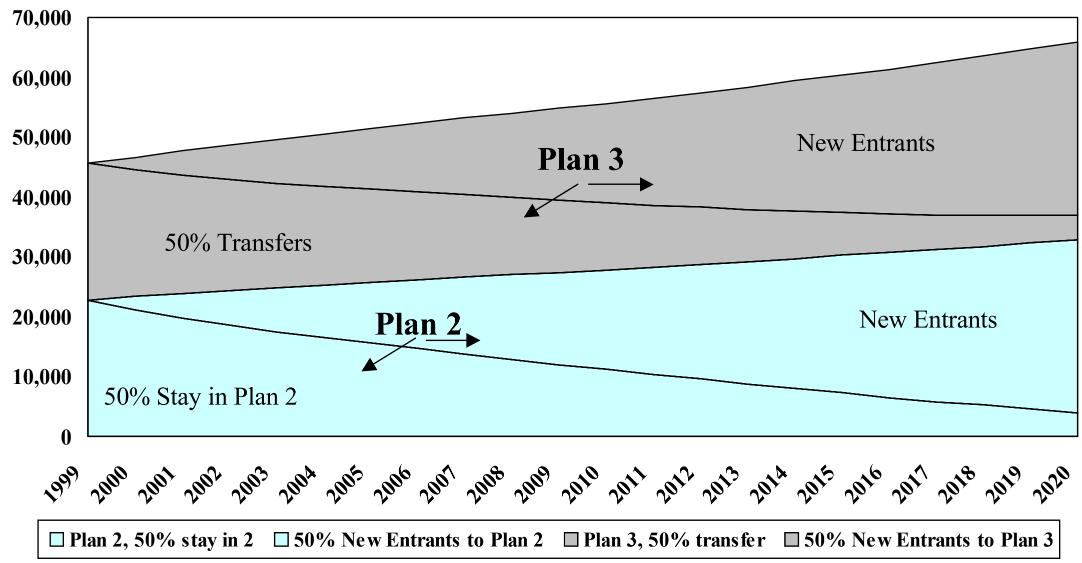
About 4,000 members enter the TRS system each year. These new members could be offered a choice between plans 2 and 3 in a manner similar to that created for new members to the PERS plan 2/3 adopted by the 2000 legislature.

In the PERS plan 2/3, new entrants to PERS are offered a 90-day period during which they have a choice of plan, and if they chose plan 3, a choice of member contribution rate to their defined contribution account. At the end of the 90-day period, if the new member has made no choice, they become members of plan 3 at the minimum employee contribution rate.

Those TRS members that entered plan 3 without a choice of plans would remain in plan 3.

SERS would be quite similar to TRS. The number of members who have entered SERS plan 3 without the choice of plan 2, and the amount of service credit members have accumulated in plan 3 is now much less than in TRS 3 because SERS 3 only recently came into effect. Over time this will change as the number of new entries into SERS plan 3 each year is significantly greater than in TRS, about 5,500 members enter each year.

Table #5
Projected SERS Membership if 50% Transfer to Plan 3



Analysis: Issues Raised by the Future Hires-only Approach

New hires in a system that adopted a future hires-only approach would be offered a choice that members hired before them did not have, raising issues of fairness. Members who were in plan 2 at the creation of plan 3 have the opportunity to transfer, raising the question of why transfers could not occur from plan 3 to plan 2.

Conversely, the date of entry often determines the benefits available to members in the Washington retirement systems. For example, members joining TRS before 1977 entered TRS plan 1, but did not have the opportunity of membership in TRS plan 2 after 1977, or TRS plan 3 after 1996.

Making TRS plan 2 or plan 3 membership a choice for new entrants would introduce a number of unknowns for the future of the TRS system. Clearly, the scenarios like that illustrated in Table 2 with the TRS plan 2 membership slowly declining would be changed. If plan 2 is available to all new members, some will take that option and plan 2 will remain a portion of the system's membership indefinitely.

It is difficult to project how many, or what type of member would choose plan 2 or plan 3.

Table #6
New entrants into TRS, SERS (PERS school district), and PERS for the 1994-1999 period

Year	TRS	SERS	PERS
1994	3,764	5,394	18,303
1995	3,732	4,758	17,263
1996	3,151	5,163	18,170
1997	3,803	5,949	19,810
1998	4,067	5,541	21,749
1999	4,319	6,206	22,817
Total	22,836	33,011	118,112

3. A Prospective Choice of Plan 2 or Plan 3 for TRS and SERS

A choice of TRS and SERS plan 2 or plan 3 could be offered both to new entrants, and to existing plan 3 members who had no choice between plan 2 and plan 3 at any time. This means that any TRS plan 2 member who transferred to plan 3 would not be offered a chance to change their mind and return to plan 2.

As a prospective choice, plan 3 members would be offered a choice to enter plan 2 and collect plan 2 service credit in the future only. Alongside their new plan 2 service, they would retain their plan 3 service from the past.

In any approach involving a choice of plans for members, the issue of making the decision a one-time, irrevocable choice is raised. Internal Revenue Service rules indicate that only offering choice on a one-time irrevocable basis is generally a requirement for qualified plans. For example, public plans are prohibited from offering an ongoing choice between member contribution rates and take home pay.

In TRS all new members have entered into plan 3 since 1996. These members have at no time in the past been offered a choice between plans. The opportunity to transfer might be similar to that offered to members of TRS and SERS plan 2 in the past.

A limited period of time would be offered after the creation of the optional plan 2/3 TRS for plan 3 members who were never offered a choice of plans to move to plan 2 for purposes of future service. No past service credit would be converted from plan 3 to plan 2.

SERS future hires and members of plan 3 who never had a choice of plan 2 or plan 3 could likewise be offered the opportunity to enter plan 2.

Each year that elapses between now and the creation of a plan 2/3 for SERS, the number of members in SERS 3 that would be eligible to move to plan 2 under this prospective-only approach would increase greatly as a percentage.

Analysis: Issues Raised by the Prospective Approach

The plan 2 and plan 3 systems were designed to offer different benefits of equal value. Depending on a member's characteristics and future expectations, one of the plans could be worth more to that individual member than the other plan.

One goal of an optional plan 2/3 is to ensure that overall members are no better and no worse off by their choice of plan 2 or plan 3. By allowing a member to retain service credit in plan 3 for their first years of employment and to accumulate plan 2 credit thereafter, that member may be left in a better position than if they had been in plan 2 from the start.

A member retaining their plan 3 credit and moving to plan 2 may be better off because the member will have the advantage of early contributions to their individual member accounts including the extraordinary gain-sharing distributions, and then years of compound returns from early contributions that provide some of the biggest advantages of the defined contribution approach.

A prospectively transferring plan 3 to plan 2 member would also have access the lower plan 2 contribution rates. These lower contribution rates are the method by which plan 2 members receive the gain-sharing distributions, so in effect the member prospectively transferring from plan 3 to plan 2 might receive this benefit more than once.

4. A Retroactive Choice of Plan 2 or Plan 3 for TRS and SERS

Such an approach allows a choice for members of TRS and SERS plan 3 who had no choice of plan 2 at any time the opportunity to move both future service and past service into plan 2. As in the two prior approaches, all future hires would also have the opportunity to choose plan 2 or plan 3 at entry.

Approximately 15,000 current plan 3 TRS members and a growing number of SERS members have never had the opportunity to become members of plan 2. These members could be offered the choice of remaining in plan 3, or transferring completely to plan 2. The TRS and SERS plan 2 members who chose to transfer to plan 3 would not have an opportunity to transfer back to plan 3.

All new members of TRS and SERS after the creation of optional plans 2/3 could be offered a choice of plans similar to what will be offered PERS members following the start of PERS plan 2/3 in March 2003.

The number of potential plan 3 to 2 transferees will grow over time, however. For example, if an optional plan 2/3 was created for both systems in 2004, then there could be about 32,000 members of TRS plan 3 who never had a choice of being part of plan 2, and there could be about 17,000-20,000 members of SERS.

Analysis: Issues Raised by the Retroactive Approach

A difference between the prospective and retroactive approaches compared in this report is dealing with the transfer of service from plan 3 to plan 2. A plan 3 to plan 2 transfer has not been a part of any of the plans created in the Washington retirement systems, and involves new and complex considerations. Many of the other issues in the prospective approach remain in the retroactive approach.

If members are to be offered an option that would leave them no better and no worse off that if they had been in plan 2 from their entry into the system, some of the same fairness issues as analyzed in the prospective approach remain, and additional issues arise.

A method for plan 3 members to transfer retroactively to plan 2, might incorporate a process to place the member in the position they would have been had they been in plan 2 since their entry into the retirement system. This could involve a transfer from the plan 3 member's individual defined contribution account to the plan 2 fund.

The different distribution of risk in the plan 2 and plan 3 designs could make the "no better off, no worse off" policy difficult to implement in some circumstances, however. A member wanting to transfer could receive a windfall, be faced with a questionable choice, or be in a position of not being able to choose at all.

Some might make a transfer from plan 3 to plan 2 and have a substantial balance remaining in their individual member account. This amount could not be distributed to the member unless the member separated from service, but would still result in a benefit for the member that they would not have if they originally entered the retirement system in plan 2.

Conversely, a plan 3 member who wants to transfer to plan 2 could conceivably not have a sufficient balance in their member account to make their transfer to plan 2 credit, despite having never withdrawn. These members might be required to make an additional contribution, or be prohibited from transferring altogether.

III. Options

A. Optional SERS and TRS Plan 2/3, Future Hires-only:

Adopts a prospective-only optional plan 2/3 for TRS, SERS, or both.

At a future date, all new entrants are offered the irrevocable choice of plan 2 or plan 3 at entry, implemented in a fashion similar to the option which will be offered new entrants to PERS plan 2/3 after that optional plan goes into effect during 2002-2003.

The only transfers between plans 2 and 3 that will be permitted are those allowed under current law, the transfer from plan 2 to plan 3 of members whose plan 2 membership predates the creation of plan 3 for their system.

B. Optional SERS and TRS Plan 2/3, Prospective Application:

Adopts an optional plan 2/3 for TRS, SERS, or both that includes a prospective aspect allowing plan 3 members who were offered no choice between plans 2 and 3 the irrevocable option of transferring to plan 3. Those choosing to transfer accumulate plan 2 credit for all future service.

All new entrants are offered the irrevocable choice of plan 2 or plan 3 at entry, implemented in a fashion similar to the option which will be offered new entrants to PERS plan 2/3 after that optional plan goes into effect during 2002-2003.

C. Optional SERS and TRS Plan 2/3, Retroactive Application:

Adopt an optional plan 2/3 for TRS, SERS, or both that includes a retroactive aspect allowing plan 3 members who were offered no choice between plans 2 and 3 the irrevocable option of transferring to plan 2. Plan 3 service credit and funds from individual member accounts are transferred to plan 2, placing transferring members in the same position as if they began retirement system participation in plan 2.

All new entrants are offered the irrevocable choice of plan 2 or plan 3 at entry, implemented in a fashion similar to the option which will be offered new entrants to PERS plan 2/3 after that optional plan goes into effect during 2002-2003.

Several types of transfers will be permitted. The current plan 2 to plan 3 transfers permitted under current law will continue.

Only those plan 3 members who first entered their system after the start of their respective plan 3, and had no choice to enter plan 2 will be able to make this transfer.

IV. JCPP Recommendation:

It was decided at the December 13, 2000 Full Committee meeting that the optional plan 2/3 for future hires bill draft presented to the committee not be recommended to the Legislature.

PERS 1 and TRS 1 30-year Cap

Background:

Benefits earned by members of the Public Employees Retirement System Plan 1 (PERS 1) and Teachers Retirement System Plan 1 (TRS 1) are statutorily limited to 60% of average final compensation. This limit is often called the "30-Year Cap" because the 2% per year benefit formula reaches its maximum at 30 years of member service. The current labor market situation is one in which labor shortages have become the norm and retirement policies are shifting to keep workers longer and ease their way into retirement.

Committee Activity:

Roundtable Discussion: PERS 1 30-year Cap and Post-retirement Employment
August 16, 2000, Full Committee Meeting
Roundtable Discussion: TRS 1 30-year Cap and Post-retirement Employment
August 16, 2000, Full Committee Meeting
Roundtable discussion: 30-year Cap / Post-retirement Employment
September 20, 2000, Full Committee Meeting
Presentation: Draft proposal, Public Testimony, Additions to proposal approved
November 15, 2000, Full Committee Meeting
Proposals Approved:
December 13, 2000, Full Committee Meeting

Recommendation to Legislature:

PERS 1 and TRS 1 members who reach their 30th year of service before or during the period from July 1, 2001 to June 30, 2005 will be eligible to earn additional service credit towards their retirement during this period to a maximum benefit of 68 percent of their average final compensation. In addition, PERS 1 and TRS 1 members who froze their average earnable compensation and placed their post-30-year contributions in a separate interest-bearing account, will be given the opportunity to rescind that election.

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PERS and TRS 1
30-Year Cap

Joint Committee on Pension Policy
Revised December 19, 2000

Prepared by:

Robert Wm. Baker
Senior Research Analyst

I. Description of the Problem Situations

Benefits earned by members of the Teacher Retirement System Plan 1 (TRS 1) and the Public Employees Retirement System Plan 1 (PERS 1) are statutorily limited to 60% of their average final compensation (AFC). This limit is oft referred to as the "30-Year Cap" because of the 2% per year benefit accrual formula that reaches a maximum at 30 years of member service. Though benefits are capped at 60% of AFC, members are required to contribute to the system as long as they are employed by the state.

The 30-year cap also produces an unusual benefit feature in TRS 1. TRS 1 members are allowed to withdraw some or all of their contributions upon retirement. If they chose to do so their monthly benefit is reduced an actuarially determined amount. There are instances where a TRS 1 member's benefit, after they withdraw their annuity, may be less with more than 30 years service than at 30 years service.

II. Background

30-Year Cap: In 1972 the Washington State Legislature increased the PERS 1 retirement allowance to the current 2% formula. At the same time, they set the maximum benefit at 60% of the member's AFC. In the next two years, the retirement allowances were increased similarly for TRS 1 and LEOFF 1 members. So all Plan 1 systems have a retirement allowance that reach their maximum after 30 years of service. Other State administered plans, both the more current plan 2/3 systems and the Washington State Patrol system, have different maximum service retirement allowances (see Figure 1).

Figure 1
Maximum Service Retirement Allowances

Plan 1 Systems — 60% of AFC
Plan 2/3 Systems — No Limit
WSPRS — 75% of Average Final Salary

A. Benefit Formula

For purposes of benefit calculations, all Plan 1 participants maximize their member service credit at 30 years. This results in a retirement benefit that reaches its maximum at 60% of a member's average final compensation (see Figure 2). This does not mean that a member's retirement allowance is set at the 30 year mark. As long as a member receives salary increases, the retirement benefit will increase accordingly.

Figure 2
How the Plan 1 Benefit Formula Works

A Plan 1 member may retire at age 55 with 25 years of service. If their Average Final Compensation (AFC) were $38,500, the calculation of their annual retirement benefit would appear thus:

2% X 25 years of service X $38,500 = $19,250

If that member stayed for another 5 years, for a total of 30 years of service, and their AFC had increased to $48,000, the calculation of their annual retirement benefit would appear thus:

2% X 30 years of service X $48,000 = $28,800

If that member stayed for another 3 years, for a total of 33 years of service, and their AFC had increased to $52,864, the calculation of their annual retirement benefit would appear thus:

2% X 30 years of service X $52,824 = $31,694

B. No Service Limit for COLA

While the Plan 1 systems do have a retirement benefit formula that reaches its maximum at 30 years of service, the calculation for a Plan 1 retiree's Uniform Cost of Living Adjustment (COLA) has no such limit. The Uniform COLA is based on the actual number of months of a member's service times the Uniform COLA amount (see Figure 3).

Figure 3
Uniform COLA Calculation

If a Plan 1 retiree had served 30 years, had been retired at least one year, and was 66 years of age, their COLA would be:

360 (30 years X 12 months) X $1.08 (the current Uniform COLA amount) = $388.80

If that same retiree had decided to stay in service two more years, their COLA would be:

384 (32 years X 12 months) X $1.08 = $414.72

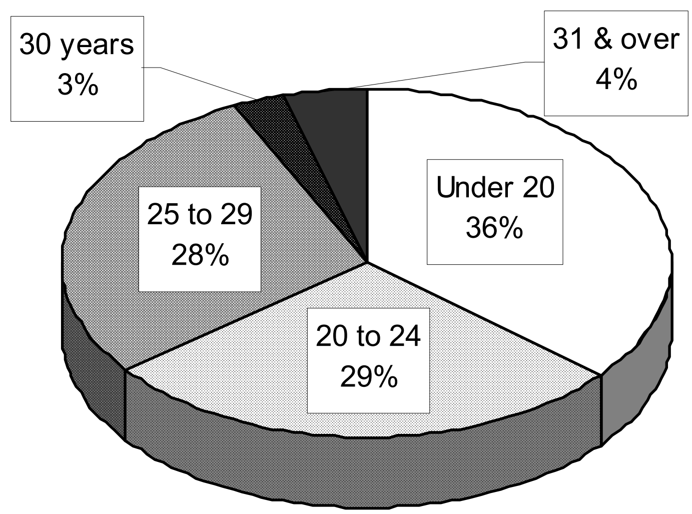
C. PERS 1 Demographics

1. *Active Members*

As of December 31, 1999 there were 28,168 active PERS 1 members. Of those, 4% had already served 31 years or more (see Figure 4). Three percent had served 30 years. Another 28% were within 5 years of reaching that 30 year mark. And 29% were within 10 years of reaching their 3rd decade of service.

Figure 4

1999 PERS 1 Active Members by Years of Service (Average years of service = 20.1)



2. *Recent Retirees*

Contrast the distribution of active members with that of retirees. Of the 1,482 PERS 1 members who retired in 1999 some 28% served 31 years or longer (see Figure 5). Fully 31% had served 30 years. 24% served between 25 and 29 years. Another 8% had between 20 and 24 years of service. And 9% of the new retirees had less than 20 years of service. So a goodly portion of PERS 1 plan members do not wait until reaching 30 years of service to retire.

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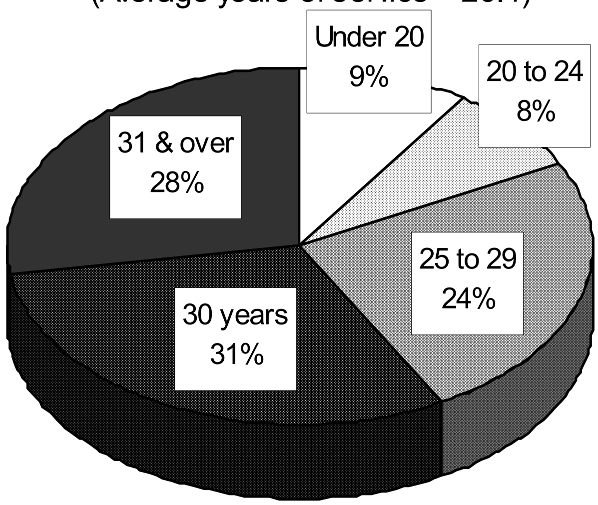
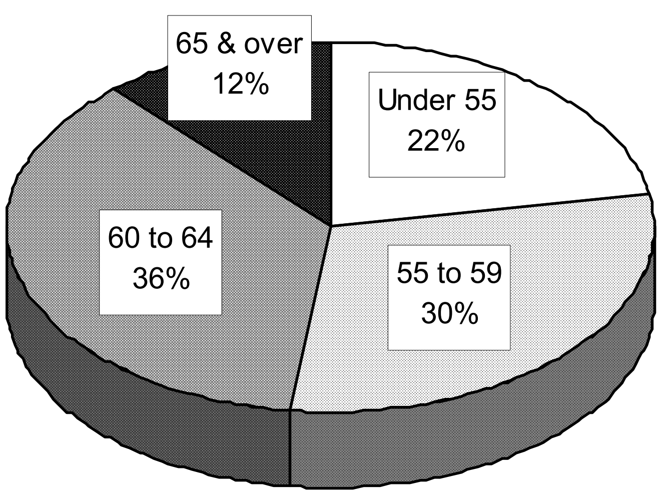
Figure 5
1999 PERS 1 Retirees by Years of Service
(Average years of service = 26.4)



3.
Age of PERS 1 Retirees

While the average age of new PERS 1 retirees was 58.8 years in 1999, the age range was quite broad. Some 22% of new retirees were less than 55 years of age (see Figure 6), with the youngest being 49. Just 12% were age 65 and over, with the oldest being 75. So many PERS 1 retirees are still of working age.

Figure 6
1999 PERS 1 Retirees by Age
(Average age = 58.8)



D. TRS 1 DEMOGRAPHICS

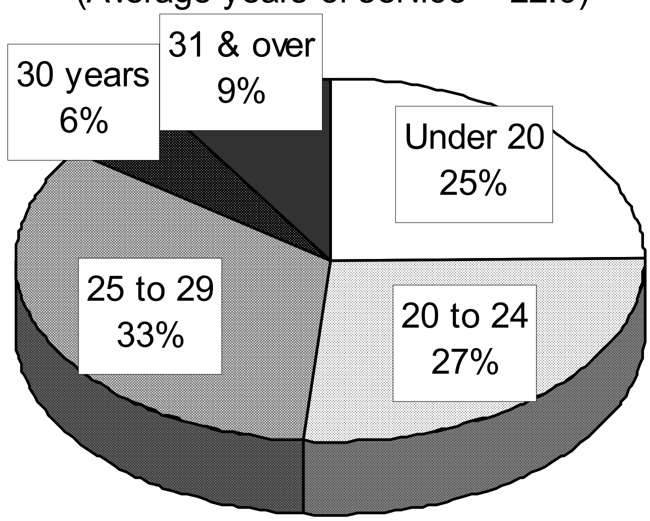
1. *Active Members*

As of December 31, 1999 there were 18,737 active TRS 1 members. Of these 9% had already served 31 years or longer (see Figure 7). Another 6% of active TRS 1 members had served 30 years. As a result, 15% of all active TRS 1 members had maximized their benefit accrual by the end of 1999. In addition, one-third of all active plan members were within 5 years of reaching their 30th year of service. That leaves 52% of plan members who had served 24 years or less.

Figure 7

TRS 1 Active Members by Years of Service

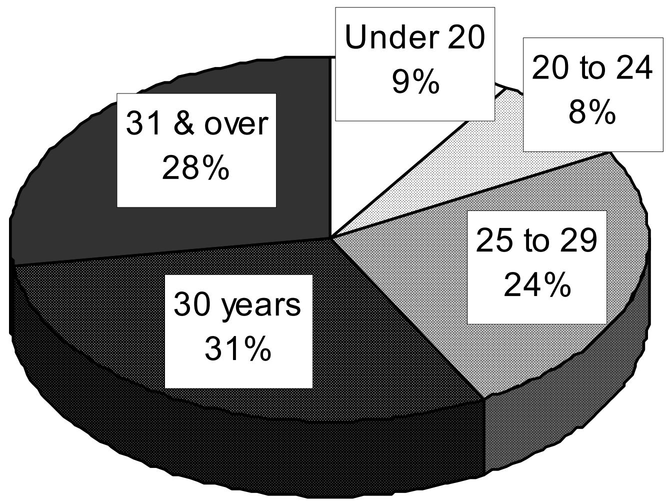
(Average years of service = 22.9)



2. **Recent Retirees**

Of the 1,359 TRS 1 members who retired in 1999, 28% had served 31 years or longer (see Figure 8). Fully 31% had served 30 years. 24% had served between 25 and 29 years. Again, there are many members who retire before reaching 30 years of service.

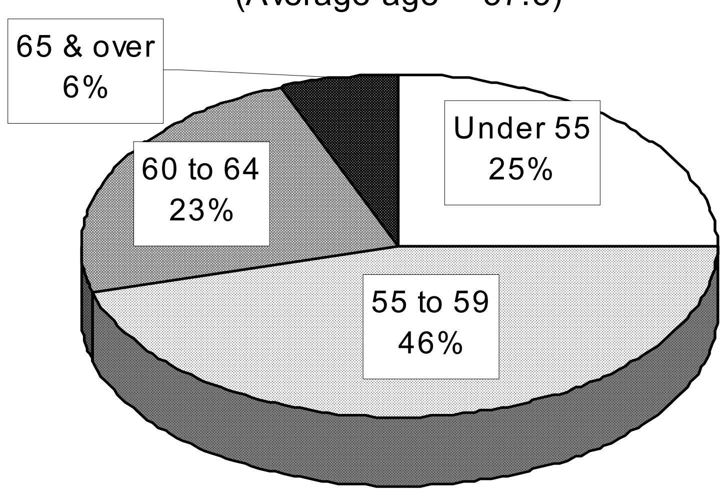
Figure 8
1999 TRS 1 Retirees by Years of Service
(Average years of service = 28.8)



3. ***Age of TRS 1 Retirees***

And as with the discussion of PERS 1 retirees, TRS 1 retirees also have an age pattern that has an impact on member's attitude towards the 60% maximum benefit / 30-year cap. As in PERS 1, many TRS 1 members retire well before passing their 60th year. Of the 1,359 TRS members who retired in 1999, fully 25% of them were age 55 or under (see Figure 9). Another 46% were age 55 to 59. Tally up those two age categories and it shows that about one in four were over the age of 60.

Figure 9
1999 TRS 1 Retirees by Age
(Average age = 57.5)



4. ***TRS 1 Benefit Anomaly***

In PERS 1, the member, upon retirement, receives a monthly benefit based on the basic Plan 1 formula. In TRS 1, members may receive a benefit based on the same formula, or they may opt to withdraw some or all of their contributions upon retirement and receive a reduced monthly benefit. The withdrawn amount and the residual benefit combined are to provide the retiree with the statutory benefit defined as 2% per year of service times the FAS. Therefore, as the value of the annuity increases, the value of the residual benefit decreases.

When a TRS 1 member withdraws their contributions, the factors used to reduce the monthly benefit introduce an age element into the calculation of the residual benefit amount. The benefit reduction is also a function of the amount of contributions a member chooses to withdraw. Because contributions build quite quickly in the latter stages of a member's service, this has a distinct bearing on how much the residual benefit is reduced. As a result, the residual benefit may be less for an older retiree than a younger retiree with the same salary and service credit. Or, if a member chooses to remain employed beyond their 30th year, their residual benefit after withdrawal may decline during their subsequent years of service.

5. ***No Pay Increase Scenario***

The following Figure 10 illustrates how the TRS 1 retirement benefit calculations can result in a lesser residual benefit if a member chooses to withdraw all of their contributions. The assumptions behind this table are that the TRS 1 member reaches their 30th year of service at age 55 and that they receive no salary increases in the years they work beyond their 30th year of service.

Figure 10

TRS 1 Benefit Analysis: No Salary Increases After 30 Years

YOS	Salary	Benefit	Employee Contributions	Reduction	Benefit After Reduction
30	$ 49,056	$ 28,800	$ 95,152	$ -8,253	$ 20,547
31	$ 49,056	$ 29,434	$ 103,409	$ -9,071	$ 20,362
32	$ 49,056	$ 29,434	$ 112,120	$ -9,954	$ 19,480
33	$ 49,056	$ 29,434	$ 121,309	$ -10,908	$ 18,526

As shown in Figure 10. . .

- Salary is constant
- Benefit increases a modest amount (AFC at the 30th year includes a somewhat smaller salary for the 29th year.)
- Employee contribution build by $26,157 between the 30th and 33rd year
- Reduction amount builds similar to the employee contributions
- Benefit after reduction declines

The situation in this scenario, where a member's salary does not increase in their latter years of employment, is relatively rare. But there are numerous instances where a member may have had a break in service for professional or family reasons. Upon returning to work they may decide to work at a lesser level. Therefore their salary can be lower in the years immediately preceding retirement than it was earlier in their career.

6. *Regular Pay Increase Scenario*

Now it is unusual for a TRS 1 member to receive no salary increases over an extended period. There certainly have been instances where State fiscal issues have severely constrained salary gains, but rarely has that extended beyond one biennium. A more realistic scenario is one in which members continue to receive small but steady salary increases.

The assumptions behind Figure 11 differ from Figure 10 only in that instead of receiving no salary increases in the years worked beyond their 30th year of service, the member continues receiving annual 3.0% increases.

Figure 11
TRS 1 Benefit Analysis:
30% Annual Salary Increases After 30 Years

YOS	Salary	Benefit	Employee Contributions	Reduction	Benefit After Reduction
30	$ 49,056	$ 28,800	$ 95,152	$ -8,253	$ 20,547
31	$ 50,528	$ 29,875	$ 103,500	$ -9,079	$ 20,796
32	$ 52,044	$ 30,771	$ 112,399	$ -9,979	$ 20,762
33	$ 53,605	$ 31,694	$ 121,885	$ -10,960	$ 20,735

As shown in Figure 11. . .

- Salary increases over $4,500 from the 30th year to the 33rd year.
- Benefit increases almost $2,900.

- Employee contribution build by $26,733 between the 30th and 33rd year.
- Reduction amount builds similar to the employee contributions.
- Benefit after reduction remains relatively constant.

7. Two Large Salary Increases Scenario

The regular pay increase scenario may be considered a more typical salary pattern, but once in a while an atypical salary increase occurs. So in this third scenario consider what would happen were a TRS 1 member to receive two substantial salary increases in their 31st and 32nd year of service.

Figure 12
TRS 1 Benefit Analysis:
6.5% of Salary Increases in Years 31 and 32

YOS	Salary	Benefit	Employee Contributions	Reduction	Benefit After Reduction
30	$ 49,056	$ 28,800	$ 95,152	$ -8,253	$ 20,547
31	$ 52,245	$ 30,390	$ 103,605	$ -9,089	$ 21,302
32	$ 55,641	$ 32,366	$ 112,733	$ -10,009	$ 22,357
33	$ 55,641	$ 33,384	$ 122,362	$ -11,002	$ 22,382

As shown in Figure 12. . .

- Salary increases almost $6,600 from the 30th year to the 32rd year.
- Benefit increases almost $4,600 from the 30th to the 33rd year.
- Employee contribution build by $27,210 from the 30th to the 33rd year.
- Reduction amount builds similar to the employee contributions.
- Benefit after reduction builds by over $1,800.

8. Considerations

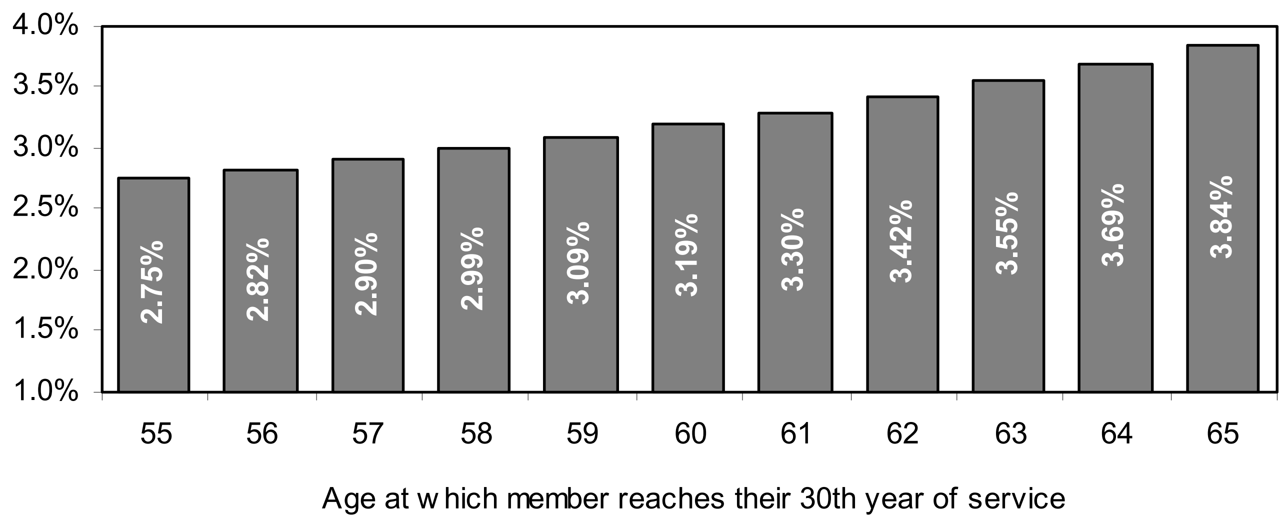
- A TRS 1 member needn't withdraw all their contributions. Should they choose to withdraw a lesser amount, then the reduction for withdrawal will also be a lesser amount.
- When a TRS 1 member withdraws their contributions, they assume responsibility for that portion of their retirement benefits.
- An older retiree can purchase a larger annuity than a younger retiree with the same withdrawn amount; a member retiring at 65 has an obviously shorter life expectancy than a member retiring at 55.

- As employee contributions accumulate more quickly in the latter years, they fund a greater portion of the member's benefit. So should they be withdrawn, they will decrease the residual monthly benefit by a larger amount.

9. ***The Age Salary Gain Dynamic***

Because of the age element incorporated in the benefit reduction factors, an unusual salary dynamic results. It has already been shown that if a TRS 1 member remains active beyond their 30th year of service, their salary must increase in order that their residual benefit not decline should they chose to withdraw all their contributions. It has also been said that an older retiree can purchase a larger annuity than a younger retiree with the same amount of money. As a result, the older a TRS 1 member, the greater the salary gain must be beyond their 30th year of service for their residual benefit to not decline should they chose to withdraw all their contributions (see Figure 13).

Figure 13
Annual Salary Gains Beyond the 30th Year of Service In Order that the Benefit After Withdrawal Not Decline



10. ***Evolution of the 30-Year Cap***

The benefit cap has been in existence since the founding of the Plan 1 systems. It has only been recently, however, that this limitation has become a open issue. It is likely that the current force of this issue results from labor market factors. By all standards, the current labor market situation is one in which labor shortages have become the norm.

While much attention has been focused on jobs in the high-tech sectors, all employers, public and private, are facing labor shortages at all skill levels. There have been many instances where human resource policies, which were established during a long period labor abundance, are not configured to deal with an endemic shortage. During periods of labor abundance recruitment policies were configured principally to filter candidates, and early retirement policies were instituted to speed workers into retirement. In today's labor shortage environment recruitment policies are shifting so as to attract candidates, and retirement policies are shifting to keep workers longer and ease their way into retirement.

IV. TRS 1 and PERS 1 30-Year Cap

A. Proposal to Temporarily Increase the Maximum Retirement Allowance in TRS 1 and PERS 1 Systems

TRS 1 and PERS 1 retirement allowances are limited to 60% of members Average Final Compensation (AFC). TRS 1 and PERS 1 retirement benefits are based on the 2% per year benefit accrual formula that reaches a maximum at 30 years of member service, hence the common parlance "30-year cap." It is usual for many TRS 1 and PERS 1 members to complain that they are being "forced" into retirement because it is not worth their while to stay longer than the 30 years at which the benefit ratio reaches its maximum. Even though members may increase their retirement benefit through the salary increases they receive after their 30th year of service, for many the benefit gain is not comparable to the allure of retirement; many members feel that their retirement is an opportunity to receive both their benefit and earn a wage in a new endeavor thus maximizing their income potential.

B. JCPP Recommendation

In recognition of the tight labor market and teacher shortage, the Executive Committee recommends temporarily lifting the 30-year Cap for active TRS 1 and PERS 1 members. Under this proposal, all members, including those with 30 or more years of service, would earn the standard 2% per year service credit over the next two biennia.

Member's Current Years of Service	Service credit if member works another 4 years
27	31
28	32
29	33
30	34
31	34
32	34

During this period, the JCPP would study the effects of this proposal.

C. Actuarial Impact:

	PERS	SERS	TRS	Total
Increase in Contribution Rates:				
Employer State	0.09%	0.09%	0.23%	
Costs (in Millions):				
2001-2003				
State:				
General Fund	$ 2.1	$ 0.9	$ 11.7	$ 14.8
Local Gov.	$ 5.0	$ 1.1	$ 2.7	$ 8.7
2001-2005				
State:				
General Fund	$ 4.7	$ 2.0	$ 25.1	$ 31.8
Local Gov.	$11.1	$ 2.3	$ 5.7	$ 19.0
2001-2017				
State:				
General Fund	$26.0	$11.0	$133.0	$170.0
Local Gov.	$61.1	$12.4	$ 30.2	$103.7

PERS 1 30-Year Cap
Bill Summary

This bill would temporarily raise the cap on PERS 1 retirement benefits — currently limited to 60 percent of a member's final average salary. This would allow all members who exceed 30 years of service before or during the next four years to accrue service credit towards their retirement benefit during those four years. As a result, PERS 1 members may be able to earn a maximum benefit of up to 68 percent of their final average salary. This is a prospective, not a retroactive bill; for those members who already have over 30 years of service credit, this would not give them credit for their current time over 30 years; they would only be eligible to earn additional service credit during the prescribed time.

This bill also provides for those who elected to freeze their average earnable compensation and place their post-30-year employee contributions in a separate interest-bearing account to be paid them upon retirement. They would have the option to rescind the election and thus earn additional service credit towards their retirement.

FISCAL NOTE

REQUEST NO.

RESPONDING AGENCY:	CODE:	DATE:	BILL NUMBER:
Office of the State Actuary	**035**	**12/6/00**	**Z-0283.1/01**

SUMMARY:

This bill impacts the Public Employees' Retirement System (PERS) Plan 1 by allowing those with over 30 years of credit to receive credit for service earned during July 1, 2001 to June 30, 2005. It also allows those who elected to receive a refund of their future contributions in lieu of including future compensation increases in the calculation of their pension, to rescind that election by December 31, 2001.

Effective Date: July 1, 2001

BACKGROUND DISCUSSION:

Currently no service credit is granted for those with over thirty years of service. This encourages retirement of these employees, particularly in years of low compensation increases.

MEMBERS IMPACTED:

As of December 31, 1999 there were 9,956 active members who had at least 25 years of service out of 28,168 active members. Any of these members who continue working during the window, and after they have 30 years of service, would get additional service credit under this bill.

The average monthly benefit for a new retiree in 1999 with 30 or more years of service was approximately $2,300 a month. If they earned the full 4 years of additional service credit, the additional benefit would be $2,300 x 34 / 30 = $2,607, ignoring future increases in benefit levels due to pay increase. Many of the members will retire before they have earned a full 4 years additional service. Others will not have 30 years at the start of the window, and will not be able to earn the full 4 years additional by the time the window closes.

Those members who do not rescind their election to receive a refund of their future contributions will receive additional service credit but the calculation of their pension will not include future pay increases.

FISCAL IMPACT:

Actuarial Determinations:

The bill will impact the actuarial funding of the system by increasing the present value of benefits payable under the System and the required actuarial contribution rate as shown below:

(Dollars in Millions)	**Public Employees' Retirement System**		
	Current	**Increase**	**Total**
Actuarial Present Value of Projected Benefits The Value of the Total Commitment to all Current Members	$12,494	$74	$12,568
Unfunded Actuarial Accrued Liability The Portion of the Plan 1 Liability that is Amortized until 2017	$1,589	$74	$1,663
Unfunded Liability (PBO) The Value of the Total Commitment to all Current Members Attributable to Past Service	$809	$72	$881
Required Contribution Rate	3.21%	.09%	3.30%

Fiscal Budget Determinations:

As a result of the higher required contribution rate, the increase in funding expenditures is projected to be:

	PERS	**SERS**
Increase in Contribution Rates:		
Employee	0.00%	0.00%
Employer State	0.09%	0.09%
Costs (in Millions):		
2001-2003		
State:		
General Fund	$ 2.1	$ 0.9
Non-General Fund	3.5	0.0
Total State	$ 5.7	$ 0.9
Local Government	$ 5.0	$ 1.1
2001-2005		
State:		
General Fund	$ 4.7	$ 2.0
Non-General Fund	7.8	0.0
Total State	$12.5	$ 2.0
Local Government	$11.1	$ 2.3

2001-2017

State:		
General Fund	$26.1	$10.9
Non-General Fund	43.1	0.0
Total State	$69.3	$10.9
Local Government	$61.4	$12.3

Gerald B. Allard, State Actuary

TRS 1 30-Year Cap
Bill Summary

This bill would temporarily raise the cap on TRS 1 retirement benefits — currently limited to 60 percent of a member's final average salary. This would allow all members who exceed 30 years of service before or during the next four years to accrue service credit towards their retirement benefit during those four years. As a result, TRS 1 members may be able to earn a maximum benefit of up to 68 percent of their final average salary. This is a prospective, not a retroactive bill; for those members who already have over 30 years of service credit, this would not give them credit for their current time over 30 years; they would only be eligible to earn additional service credit during the prescribed time.

This bill also provides for those who elected to freeze their average earnable compensation and place their post-30-year employee contributions in a separate interest-bearing account to be paid them upon retirement. They would have the option to rescind the election and thus earn additional service credit towards their retirement.

FISCAL NOTE

REQUEST NO.

RESPONDING AGENCY:	CODE:	DATE:	BILL NUMBER:
Office of the State Actuary	**035**	**12/5/00**	**Z-0275.2/01 2nd Draft**

SUMMARY:

This bill impacts the Teachers' Retirement System (TRS) Plan 1 by allowing those with over 30 years of credit to receive credit for service earned during July 1, 2001 to June 30, 2005. It also allows those who elected to receive a refund of their future contributions in lieu of including future compensation increases in the calculation of their pension, to rescind that election by December 31, 2001.

Effective Date: July 1, 2001

BACKGROUND DISCUSSION:

Currently no service credit is granted for those with over thirty years of service. This encourages retirement of these employees, particularly in years of low compensation increases.

MEMBERS IMPACTED:

As of July 1, 1999 there were 9,099 active members who had at least 25 years of service out of 18,737 active members. Any of these members who continue working during the window , and after they have 30 years of service, would get additional service credit under this bill.

The average monthly benefit for a new retiree in 1999 with 30 or more years of service was approximately $2,000 a month. If they earned the full 4 years of additional service credit the additional benefit would be $2,000 x 34 / 30 = 2,267, ignoring future increases in benefit levels due to pay increase. Many of the members will retire before they have earned a full 4 years additional service. Others will not have 30 years at the start of the window, and will not be able to earn the full 4 years additional by the time the window closes.

Those members who do not rescind their election to receive a refund of their future contributions will receive additional service credit but the calculation of their pension will not include future pay increases.

FISCAL IMPACT:

Actuarial Determinations:

The bill will impact the actuarial funding of the system by increasing the present value of benefits payable under the System and the required actuarial contribution rate as shown below:

(Dollars in Millions)	**Current**	**Increase**	**Total**
Actuarial Present Value of Projected Benefits The Value of the Total Commitment to all Current Members	$10,382	$85	$10,467
Unfunded Actuarial Accrued Liability The Portion of the Plan 1 Liability that is Amortized until 2017	$1,263	$85	$1,348
Unfunded Liability (PBO) The Value of the Total Commitment to all Current Members Attributable to Past Service	$9,359	$62	$9,421
Required Contribution Rate	5.38%	.23%	5.61%

Fiscal Budget Determinations:

As a result of the higher required contribution rate, the increase in funding expenditures is projected to be:

Increase in Contribution Rates:	
Employee	0.00%
Employer State	0.23%
Costs (in Millions):	
2001-2003	
State:	
General Fund	$11.7
Non-General Fund	0.0
Total State	**$11.7**
Local Government	$2.7
2001-2005	
State:	
General Fund	$25.1
Non-General Fund	0.0
Total State	**$25.1**
Local Government	$5.7

2001-2017

State:	
General Fund	$133.0
Non-General Fund	0.0
Total State	**$133.0**
Local Government	$30.2

Gerald B. Allard, State Actuary

PERS, TRS 2/3, and SERS Post-retirement Employment

Background:

The provisions governing the amount of time a retired PERS, TRS 2/3, or SERS member can work in a post-retirement situation are very explicit, as are the penalties for exceeding those limits. Members of these plans may work an unlimited amount for a private employer, but should they return to a temporary position with a public employer covered by their retirement plan, the limit is 5 months. The 5-month allotment has been interpreted so as to debit a month from the allotment should a retiree work just one day in a month.

Committee Activity:

Roundtable Discussion: PERS 1 30-year cap and post-retirement employment
August 16, 2000, Full Committee Meeting
Roundtable Discussion: 30-year Cap / Post-retirement employment
September 20, 2000, Full Committee Meeting
Presentation: Proposal, Public Testimony
November 15, 2000, Full Committee Meeting
Presentation - Proposal Approved:
December 13, 2000, Full Committee Meeting

Recommendation to Legislature:

Translate the 5-month post-retirement allotment into 867 hours for PERS, TRS 2/3, and SERS plans. Allow PERS, TRS 2/3, and SERS retirees to work for any PERS, TRS, SERS, or LEOFF employer in a post-retirement situation. Allow a PERS 2 retiree who was last employed by a school district or educational service district to transfer membership and service credit into SERS 2 if they rescind their retirement and return to work.

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Post-Retirement Employment

Joint Committee on Pension Policy
Revised January 4, 2001

Prepared by:

Robert Wm. Baker
Senior Research Analyst

I. Description of the Problem Situations

Because of the limit on benefit accrual, many Plan 1 members often desire to continue working after retirement. Many teachers fulfill this desire by doing what they always have done — teach — but as "on-call" substitutes or as short-term "contract" teachers, administrators, or principals. And many PERS 1 retirees continue working as well, either at a new career or in short-term project positions in Washington state government agencies.

The provisions governing the amount of time a retired TRS, PERS, or SERS member can work are very explicit, as are the penalties for exceeding those limits. There are, however, inconsistencies within and between these plans. The hours a TRS 1 retiree may work differs by the kind of position (teacher compared to administrator) and by the formality of employment relationship (contract teacher compared to on-call substitute teacher.) For PERS, TRS 2/3, or SERS retirees, the limit on how much they are allowed work is not disagreeable, but rather the method by which it is measured is what is contentious.

II. Background

A. Post Retirement Employment

1. *PERS, TRS 2/3, and SERS Post-retirement Employment*

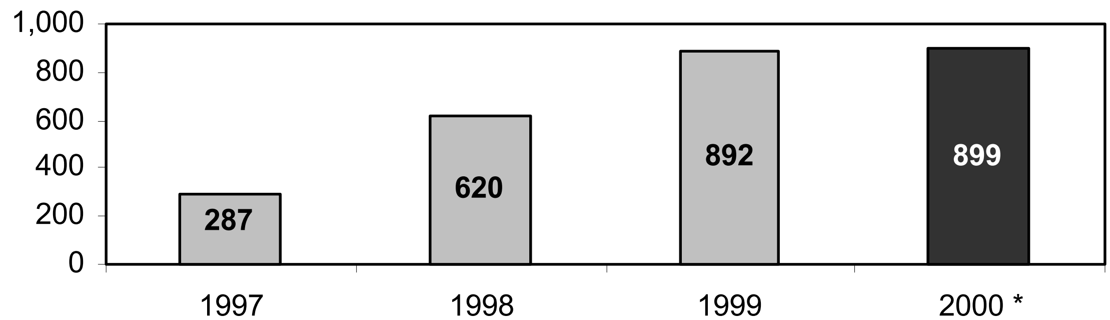
After separation from employment for at least one month, PERS, TRS 2/3, and SERS retirees are allowed to work 5 months per calendar year in an eligible position — about 42% of a calendar year — without any loss of their benefits. Unlike the detailed measurement of TRS 1 retirees post-retirement employment, PERS, TRS 2/3, and SERS retirees are subject to an unusually restrictive process of measurement. Any amount of time worked in any month will debit that month from the 5 month allotment.

Eligible Position

An eligible position normally requires five or more months of service a year for which regular compensation for at least seventy hours is earned. Any position occupied by an elected official or person appointed directly by the governor, or appointed by the chief justice of the supreme court under RCW 2.04.240(2) or 2.06.150(2), for which compensation is paid.

The measurement process for PERS,TRS 2/3, and SERS retirees effectively limits the kind of employment in which they may engage. Unlike retired TRS 1 members who may work 1 or 2 hours per day, if they so chose, PERS,TRS 2/3, and SERS retirees are limited to a full-time, part-year employment relationship. Unlike TRS 1 retirees, PERS,TRS 2/3, and SERS retirees have no real substantive choice in the amount they may work in a given month. With the understanding that any amount worked in any month will debit that month from their 5-month allotment, the vast majority of PERS,TRS 2/3, and SERS retirees are limited to a full-time, part-year arrangement.

Figure 1
PERS 1 Retirees Returning to Work in Eligible Positions by Year



* Only 6 months of data for 2000

The provisions for the reduction of benefits for surpassing the 5-month limit are so severe that the number of suspensions is quite small. Only 31 PERS 1 retirees who had returned to work in eligible positions in 1999 had their benefits suspended for working past the 5-month limit. In the first 6 months of 2000 just 21 had their benefits suspended.

Current retirees desire a "transitional" period to allow them to ease into retirement; working in a part-time capacity. At this time, however, it is not realistic for either the retirees to ask for such an arrangement, or for State Agencies to grant them.

There are other restrictions on post-retirement employment in the PERS, TRS 2/3, and SERS plans. A retiree from any of these plans may work an unlimited amount in a private sector job without the loss of any benefits. However, should a retiree choose to return to a temporary job in one of Washington's many public sector employers, their benefits would be suspended were that employer not of the same plan, i.e. a PERS retiree may only return to work for a PERS employer. The School Employees

Retirement System is a good illustration of how this can be rather complicated: Prior to the creation of SERS, classified staff in school districts and educational service districts were covered under PERS. A PERS retiree whose last employer was a school district, under current law, cannot now accept a temporary job with a school district because school districts are now SERS employers.

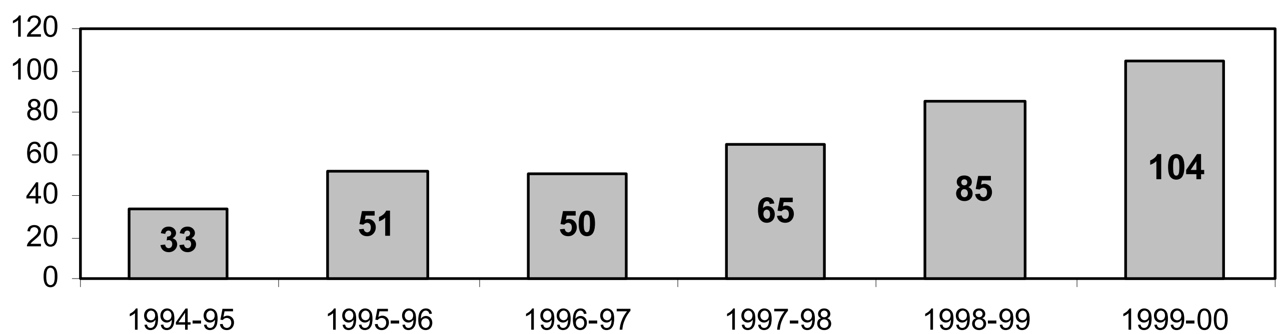
The issue is similar for PERS retirees who may wish to leave retirement to earn additional service credit. If their last employer was a school district or educational service district, and is now under SERS instead of PERS, the reitree would be unable to rescind their retirement and return to work for their last employer.

2. ***TRS 1 Post-retirement Employment***

The limits on post-retirement employment for TRS 1 members had been set at 75 days — approximately 42% of a school year. It was changed to an hourly measurement (525 hours) because in many instances substitutes and contract teachers in secondary schools do not teach an entire day, but rather may teach one or two classes per day.

In 1994, because of teacher shortages in many regions of the state, the legislature increased the number of hours on-call substitutes could work. School districts could submit resolutions declaring shortages of substitute teachers and many have done so (see Figure 2).

Figure 2
Substitute Teacher Resolutions by School Year



By submitting a resolution, school districts are allowed to increase the total hours a substitute teacher or principal can work to 840 -- to about 67% of the school year. In addition, they are allowed to increase the hours a substitute administrator or vice principal can work to 630 -- to about 50%

of the school year. But regardless of the increases in hours available for on-call substitutes, those working under contract are still limited to 525 hours.

There are 296 school districts in Washington State, so as of the 1999-2000 school year over one-third were filing shortage resolutions. This can be interpreted in a number of ways:

- The burgeoning economy may have enticed regular substitutes and other potential teachers (non-retirees) into better paying fields forcing school districts to turn increasingly to retirees to fill their substitute lists.
- It may be simply easier to recruit known entities (recent retirees) than screen new teacher candidates through the substitute lists.
- Increased use of leave benefits during the school year has boosted the total demand for substitutes, and retirees represent a readily available pool.

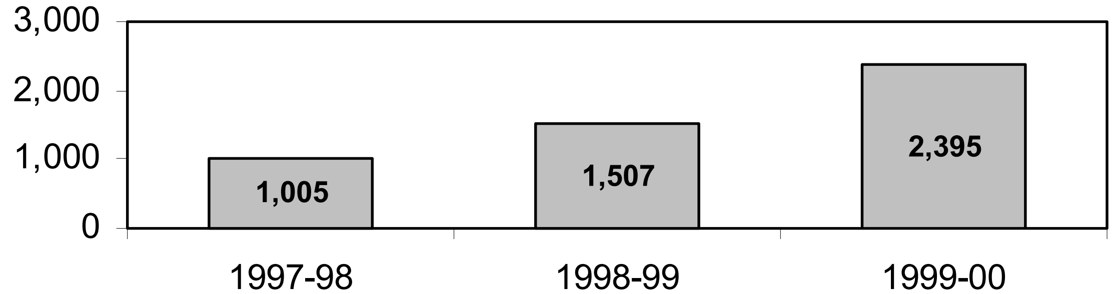
On-Call vs. Contract

There is an important distinction between working **on-call** and working **under contract**. Substitutes in on-call situations are considered to be in informal employment relationships. The informality is characterized by the fact that they have no set work schedule. On-call substitutes are typically placed on a "substitute list" from which they are chosen when a regular teacher is gone; as a result, they may work several days a week or not at all. In contrast, those working under contract are engaged in what is considered "regular" employment, similar to active TRS 1 members. They have a formal employment relationship characterized by a set work schedule.

3. TRS 1 Retirees Working

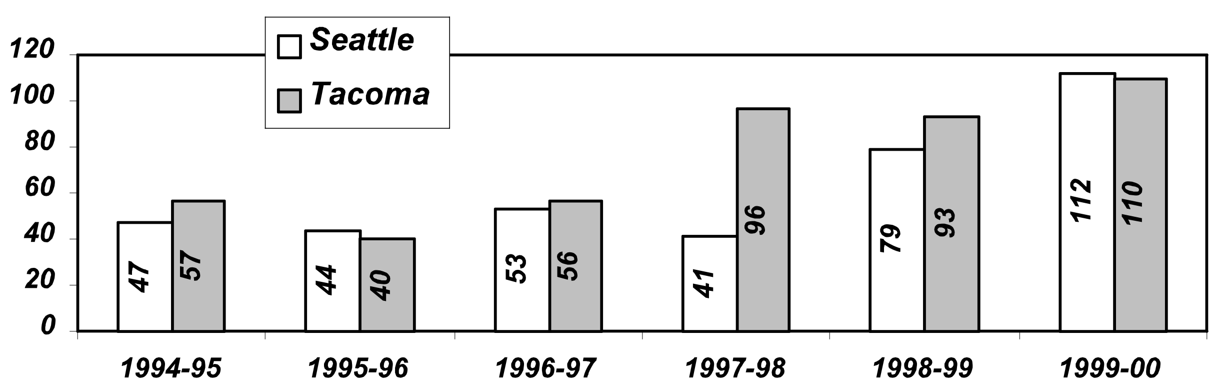
The number of TRS 1 retirees returning to work in teaching positions has grown significantly over the past several school years. During the 1997-1998 school year, just over 1,000 TRS 1 retirees were working as substitute teachers (see Figure 3). By the 1999-2000 school year that had over doubled to almost 2,400.

Figure 3
TRS 1 Retiree Substitutes by School Year



The shortage of substitutes has been felt similarly across the State but for different reasons. It would be expected that the larger metropolitan areas, though more desirable, would have difficulty attracting new teachers because of their higher cost of living (see Figure 4). And the smaller rural areas would continue to have difficulty because of their lack of amenities.

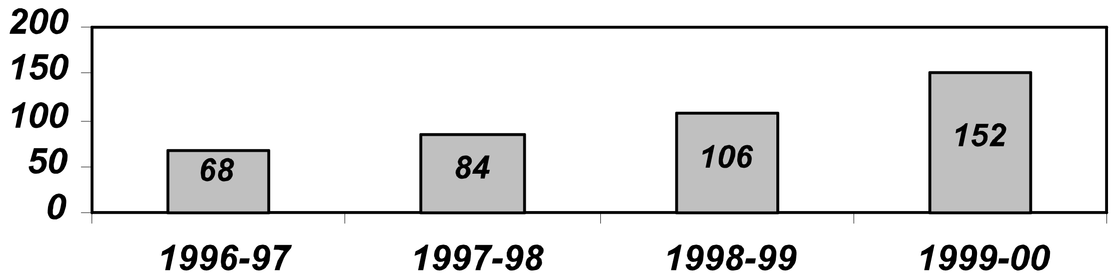
Figure 4
TRS 1 Retiree Subsitutes by Select School District



4. ***Benefits Suspended***

The increased use of retirees in on-call substitute and contract substitute positions is also seen in the number of retirement benefits that are suspended. This is, again, a very small number; the severity of the penalty for surpassing the hourly limit is such that it is relatively uncommon. Nonetheless, the number of suspensions has over doubled in the past three years (see Figure 5).

Figure 5
TRS 1 Pensions Suspended by School Year



5. ***Shifting Labor Markets***

An important factor that has likely given these issues their immediacy is the current labor market situation. In the last three calendar years, the unemployment rate in Washington State has been below 5%. Such a pattern of labor market tightness has not been experienced since the Korean War. Following the early 1950s the advent of such low unemployment has been an indicator of the peak of the business cycle. From the mid 1950s through the mid 1990s, the jobless rate in Washington had never attained such a low level for longer than one calendar year.

It was during the late 1960s through the early 1980s that the Baby-Boom generation entered the work force, thus creating an abundant supply of labor. It was also during this period that many more women joined the work force, further enhancing the labor supply. Contrast that with the more current situation where, as a result of a much lower birth-rates during the 1970s and 1980s, the availability of new entrants to the labor force has fallen markedly.

For these reasons, the current labor market situation may be considered endemic. No longer is the 5% unemployment rate an indicator of the business cycle peak, but rather is a result of significant demographic shifts. This is likely to drive equally significant changes in public and private human resource policies; policies that were established during the long period of labor abundance. Thus the playing field has changed form one in which employers had the advantage of abundant labor, to one in which new labor force participants have the advantage of their relative scarcity.

B. Prior Legislation

In an effort to assist those in the Plan 1 systems, the JCPP sponsored legislation that allowed PLAN 1 members to receive a refund of the contributions they made after 30 years of service. Members participating in this option would have their post-30-year contributions held in an interest-bearing account, and those moneys would be refunded to the member upon their retirement. Participants of the program earn 7.5% interest on their post 30-year contributions. Member's participating in this option have their benefits locked in based on earnings made at the time of participation. And members cease to accrue service credit after electing this option.

III. Proposals

A. Proposal to Modify the five month Limit on Post-retirement Employment

According to statute, PERS, SERS and TRS Plans 2/3 retirees are allowed to work 5 months per calendar year in an eligible position without loss of retirement benefits. At this time, those statutes have been interpreted very narrowly; if a retiree works a day in a given month, that month is debited from their 5-month allotment. This limits the kind of employment relationship in which a PERS, SERS and TRS Plans 2/3 retirees and employers may engage — short-term, full-time.

Contrast that with the method Department of Retirement Systems (DRS) uses to measure Teachers Retirement System Plan 1 member's post-retirement employment activity. A TRS 1 retiree may work 525 hours per year under contract or as an on-call substitute without the loss of benefits. Substitutes may even work longer (up to 840 hours) if a substitute teacher shortage resolution is filed by a school District with the DRS. Only when the retiree reaches or surpasses their allotted hours does the school district contact DRS. If the retiree has surpassed their allotted hours, the department will adjust or suspend their retirement benefit accordingly.

JCPP Recommendation:

It is the opinion of the Executive Committee that PERS, SERS and TRS Plans 2/3 retirees should be allowed to engage in employment relationships similar to that of TRS 1 retirees. As a result, The Executive Committee of the Joint Committee on Pension Policy recommends that PERS, SERS and TRS Plans 2/3 retirees be able to work up to 867 hours per calendar year without loss of retirement benefits.

Actuarial Impact: None.

B. Proposal to Increase the Allowable Hours of TRS 1 Retirees in Select On-Call and Contract Positions.

The limits on post-retirement employment for TRS 1 members originally had been set at 75 days, or approximately 40% of a school year, that a member could work without a reduction of pension. It was later changed to an hourly measurement (525 hours) because in many instances substitutes and contract teachers do not teach an entire day, but rather may teach one or two classes per day in secondary schools.

In 1994, because of teacher shortages in many regions of the state, the law was amended so as to allow retiree on-call substitute teachers, administrators, and principals to work a greater number of hours during the school year. School districts could submit resolutions to DRS declaring shortages of certified staff. In doing so they were allowed to increase the total hours an on-call substitute teacher or a substitute principal could work by 315 to a total of 840. Similar resolutions allowed school districts to increase the hours a substitute administrator or vice principal could work by 105 hours to a total of 630. But regardless of the increases in hours allowed for on-call substitutes, those working under contract were still limited to 525 hours.

JCPP Recommendation:

In recognition of teacher shortages in many school districts and in order to achieve greater consistency the Executive Committee of the Joint Committee on Pension Policy recommends that school districts be allowed to engage the services of TRS 1 retirees, either as on-call substitutes or under contract, using the same hourly allotments.

Substitute Positions	**Existing Statute**		**Proposed Statute**
	Standard	Additional with Shortages	Standard
On-call Teacher	525	315	840
On-call Administrator	525	105	840
On-call Vice Principal	525	105	840
On-call Principal	525	315	840
Under Contract	525	0	840

Actuarial Impact: None.

PERS, TRS 2/3 and SERS Post-retirement Employment
Bill Summary

This bill translates the current five-month post-retirement allotment that retirees may work without loss of benefits in the PERS, TRS 2/3, and SERS chapters into 867 hours (5/12 x 2080 hours). Currently, the 5-month allotment has been interpreted so as to debit one month from that allotment if a retiree works but one day in a month. This limits the kind of employment relationship in which retirees and employers may engage -- that of short-term, and full-time. The use of an hourly measure would allow retirees and employers greater flexibility in establishing post-retirement work schedules.

The bill would also eliminate certain restrictions on where retirees may work in a post-retirement situation. Currently, should a retiree chose to accept a post-retirement position within government, they are limited to those employers under their retirement plan -- a PERS retiree may only work for a PERS employer -- otherwise their retirement benefits are suspended. This bill would allow retirees from one plan to work for an employer under another plan -- a PERS retiree would be able to work for a SERS employer.

The bill would also allow a PERS 2 retiree, whose last employer was a school district or educational service district, to transfer their membership and service credit to SERS 2 should they wish to resume employment and earn additional service credit.

FISCAL NOTE

REQUEST NO.

RESPONDING AGENCY:	CODE:	DATE:	BILL NUMBER:
Office of the State Actuary	**035**	**01/04/01**	**Z-0323.1/01**

SUMMARY:

This bill impacts the Teachers Retirement System (TRS) Plan 2/3, Public Employees Retirement System (PERS) Plans 1 and 2/3, and School Employees Retirement System(SERS) Plan 2/3 by limiting the number of hours a retiree may work without a suspension of their benefits to 867 hours.

Effective Date: 90 days after session.

BACKGROUND DISCUSSION:

The current limit is 5 months.

MEMBERS IMPACTED:

Few members exceed the limit as now exists. Little change in the number of pensions suspended should result with this change since this will allow employees to work more hours without a change in their work schedule.

Some members will be able to work more hours than before without a suspension of their benefits. Some will be able to work the same number of hours they were working before they retired. This may encourage some members to retire earlier and return to work to collect both a pension and a paycheck. This would be especially true for someone who is eligible for an unreduced pension (age 65 with 5 years of service) or eligible for the 3% early retirement factor (age 55 with 30 years of service).

FISCAL IMPACT:

This would not generate an immediate increase in contribution rates, since the cost impact is not determinable without more information regarding how many active employees would take advantage of it and how much earlier they might retire.

Rather the cost would emerge as a loss to the system as more participants retiree than expected.

There is no increase in contribution rates and thus no increase in funding for the biennium.

Gerald B. Allard, State Actuary

Public Safety Benefits

Background:

Enforcement officials of certain state agencies and other Public Employees Retirement System (PERS) members working in hazardous occupations have supported changes to the eligibility criteria for Law Enforcement Officers' and Fire Fighters' System (LEOFF) plan 2 membership. These groups include:

> Department of Fish and Wildlife, Department of Natural Resources, State Parks and Recreation Commission, Department of Social and Health Services, State Gambling Commission, State Lottery Commission, State Utilities and Transportation Commission, State Liquor Control Board, State Department of Correction, and Public Utility District journeyman outside electrical workers.

Discussions during the 2000 interim included proposals that would provide supplemental benefits within PERS, instead of moving PERS members into LEOFF.

Committee Activity:

Roundtable Discussion:
  August 16, 2000, Full Committee Meeting
Presentation:
  November 15, 2000, Full Committee Meeting

Recommendation to Legislature:

None.

Staff Contact:

David Pringle – 586-7616 – pringle_da@leg.wa.gov

Public Safety Benefits

Two Possible Approaches to Providing Public Safety Benefits in PERS 2/3:

Two possible approaches that could be taken in the area of public safety benefits for PERS involve the creation of supplemental benefits, paid for by additional contributions by members and employers, for certain members in public safety positions.

A defined benefit and a defined contribution approach are each described below. In each case, the additional contributions could be used to fund a reduction in the early retirement reduction factor from the current actuarial rate (or 3% after age 55 with 30 years of service), to a 3% rate after the indicated member age and years of service.

The public safety positions that might be part of the supplemental benefit program include those now specifically listed as limited authority law enforcement officers in the LEOFF chapter, chapter 41.26 RCW, including enforcement officers with the state departments of natural resources, fish and wildlife, corrections, social and health services; the state gambling, lottery and parks and recreation commissions; the state liquor control board and also certificated journeyman outside electrical workers employed by Public Utility Districts.

A. Defined Benefit Approach:

Create a supplemental defined benefit for members in the defined public safety positions.

The supplemental defined benefit might be comprised of mandatory additional employer and employee contributions that would be used to reduce the early retirement reduction factor for the covered employees from the full actuarial rate to a 3% rate at a lower age and service level than currently available in PERS.

1. 3% ERRF at age 55, 25 years of service - approximate 1% total contribution rate.

2. 3% ERRF at age 55, 20 years of service - approximate 2% total contribution rate.

If a member is in plan 2, the additional contribution rate is paid by both the employee and the employer, improving the reduction factor on the 2% per year of service defined benefit. If a member is in plan 3, the additional contribution rate is paid only by the employer, and it serves only to improve the reduction factor on the 1% formula defined benefit portion.

B. Defined Contribution Approach:

Create a supplemental defined contribution benefit for PERS 2/3 members in the defined public safety positions. The accumulated defined contributions could be used to “purchase” an improved early retirement reduction factor of the amounts illustrated in examples 1 and 2 below.

Regardless of the member’s decision to purchase the ERRF, the additional contributions would be available to them as a defined contribution amount at retirement, similar to the existing plan 3 individual member account.

The defined contribution benefit might be comprised of mandatory additional employer and employee contributions to a defined contribution account. The benefit program could begin at the time the PERS plan 2/3 benefit is available to all new PERS members, the opening of the local government window of PERS 2/3, September 1, 2002.

1. 3% ERRF at age 60 - Approximate additional contribution rate: 5%.

2. 3% ERRF at age 62 - Approximate additional contribution rate: 3.5%.

If a member is in plan 2, both the employer and employee pay the additional defined contribution, and the two amounts will be available to improve the ERRF on the plan 2 2% per year of service defined benefit. If the member is in plan 3, only the employer need make the additional contribution, and this amount will be available to improve the ERRF on the plan 3 1% per year of service defined benefit.

SERS Correcting Amendments

Background:

Several statutory sections relating to the retirement systems needing correction were identified by the Office of the State Actuary, the Department of Retirement Systems, and the State Investment Board during the 2000 interim.

Committee Activity:

Presentation: SERS Technical Corrections
November 15, 2000, Full Committee Meeting
Proposal Approved:
December 13, 2000, Full Committee Meeting

Recommendation to Legislature:

Five sections suggested for correction by the Office of the State Actuary, the Department of Retirement Systems, and the State Investment Board are amended.

Staff Contact:

David Pringle – 586-7676 – pringle_da@leg.wa.gov

SERS Correcting Amendments
Bill Summary

Several issues in the School Employees Retirements System (SERS) are corrected by amending provisions of the SERS, funding and defined contribution chapters.

A difference that developed from two bills amending a SERS-related subsection of the funding chapter during the 2000 Legislative Session is corrected making provisions that come back into effect in 2002 consistent with current law.

The State Investment Board is able to declare monthly unit values for individual account funds held for SERS, TRS, and PERS plan 3 members.

A PERS 1 definition for "totally incapacitated for duty" inadvertently included in SERS is deleted. A section allowing an election of membership prior to 1988 is decodified. The SERS chapter is added to a list of the chapters wherein, notwithstanding any other provision, a retired or disabled member is prohibited from becoming a member of another state system or plan.

SERS Correcting Amendments
Sectional Analysis

Several issues in the School Employees Retirements System (SERS) are corrected by amending provisions of the SERS, funding and defined contribution chapters.

Sec. 1. A difference that developed from two bills amending a SERS-related subsection of the funding chapter during the 2000 Legislative Session is corrected making provisions that come back into effect in 2002 consistent with current law.

Sec. 2. The State Investment Board is able to declare monthly unit values for individual account funds held for SERS, TRS, and PERS plan 3 members.

Sec. 3. A PERS 1 definition for "totally incapacitated for duty" inadvertently included in SERS is deleted.

Sec. 4. A section allowing an election of PERS membership prior to 1988 is decodified.

Sec. 5. The SERS chapter is added to a list of the chapters wherein, notwithstanding any other provision, a retired or disabled member is prohibited from becoming a member of another state system or plan.

TRS 1 Post-retirement Employment

Background:

Many TRS 1 members retire at an age where they often continue working. Many do in their retirement what they always have done — teach — but as "on-call" substitutes or as short-term "contract" teachers. Other TRS 1 retirees also work in temporary school administrator or principal positions. The provisions governing the amount of time a retired TRS 1 member can work are very explicit, as are the penalties for exceeding those limits. There are, however, inconsistencies within this plan. The hours a TRS 1 retiree may work differ by the kind of position (teacher compared to administrator), by the formality of employment relationship (contract teacher compared to on-call substitute teacher), and by the existence of personnel shortages.

Committee Activity:

Roundtable Discussion: TRS 1 30-year Cap and Post-retirement Employment
July 19, 2000, Full Committee Meeting
Roundtable Discussion: 30-year Cap / Post-retirement Employment
September 20, 2000, Full Committee Meeting
Presentation - Proposal Approved: TRS 1 Substitutes
November 15, 2000, Full Committee Meeting

Recommendation to Legislature:

Standardize the post-retirement hourly allotments for all TRS 1 retirees at 840 hours regardless of personnel shortages.

Staff Contact:

Robert Wm. Baker – 586-9237 – baker_bo@leg.wa.gov

Post-Retirement Employment

Joint Committee on Pension Policy
Revised January 4, 2001

Prepared by:

Robert Wm. Baker
Senior Research Analyst

I. Description of the Problem Situations

Because of the limit on benefit accrual, many Plan 1 members often desire to continue working after retirement. Many teachers fulfill this desire by doing what they always have done — teach — but as "on-call" substitutes or as short-term "contract" teachers, administrators, or principals. And many PERS 1 retirees continue working as well, either at a new career or in short-term project positions in Washington state government agencies.

The provisions governing the amount of time a retired TRS, PERS, or SERS member can work are very explicit, as are the penalties for exceeding those limits. There are, however, inconsistencies within and between these plans. The hours a TRS 1 retiree may work differs by the kind of position (teacher compared to administrator) and by the formality of employment relationship (contract teacher compared to on-call substitute teacher.) For PERS, TRS 2/3, or SERS retirees, the limit on how much they are allowed work is not disagreeable, but rather the method by which it is measured is what is contentious.

II. Background

A. Post Retirement Employment

1. *PERS, TRS 2/3, and SERS Post-retirement Employment*

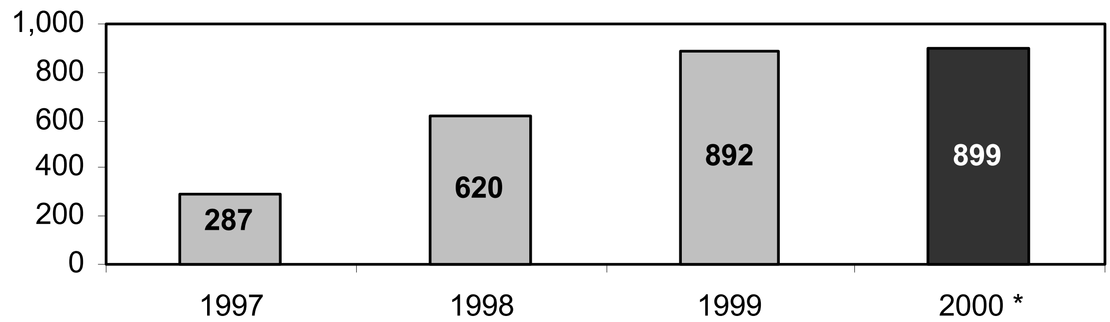
After separation from employment for at least one month, PERS, TRS 2/3, and SERS retirees are allowed to work 5 months per calendar year in an eligible position — about 42% of a calendar year — without any loss of their benefits. Unlike the detailed measurement of TRS 1 retirees post-retirement employment, PERS, TRS 2/3, and SERS retirees are subject to an unusually restrictive process of measurement. Any amount of time worked in any month will debit that month from the 5 month allotment.

Eligible Position

An eligible position normally requires five or more months of service a year for which regular compensation for at least seventy hours is earned. Any position occupied by an elected official or person appointed directly by the governor, or appointed by the chief justice of the supreme court under RCW 2.04.240(2) or 2.06.150(2), for which compensation is paid.

The measurement process for PERS,TRS 2/3, and SERS retirees effectively limits the kind of employment in which they may engage. Unlike retired TRS 1 members who may work 1 or 2 hours per day, if they so chose, PERS,TRS 2/3, and SERS retirees are limited to a full-time, part-year employment relationship. Unlike TRS 1 retirees, PERS,TRS 2/3, and SERS retirees have no real substantive choice in the amount they may work in a given month. With the understanding that any amount worked in any month will debit that month from their 5-month allotment, the vast majority of PERS,TRS 2/3, and SERS retirees are limited to a full-time, part-year arrangement.

Figure 1
PERS 1 Retirees Returning to Work in Eligible Positions by Year



* Only 6 months of data for 2000

The provisions for the reduction of benefits for surpassing the 5-month limit are so severe that the number of suspensions is quite small. Only 31 PERS 1 retirees who had returned to work in eligible positions in 1999 had their benefits suspended for working past the 5-month limit. In the first 6 months of 2000 just 21 had their benefits suspended.

Current retirees desire a "transitional" period to allow them to ease into retirement; working in a part-time capacity. At this time, however, it is not realistic for either the retirees to ask for such an arrangement, or for State Agencies to grant them.

There are other restrictions on post-retirement employment in the PERS, TRS 2/3, and SERS plans. A retiree from any of these plans may work an unlimited amount in a private sector job without the loss of any benefits. However, should a retiree choose to return to a temporary job in one of Washington's many public sector employers, their benefits would be suspended were that employer not of the same plan, i.e. a PERS retiree may only return to work for a PERS employer. The School Employees

Retirement System is a good illustration of how this can be rather complicated: Prior to the creation of SERS, classified staff in school districts and educational service districts were covered under PERS. A PERS retiree whose last employer was a school district, under current law, cannot now accept a temporary job with a school district because school districts are now SERS employers.

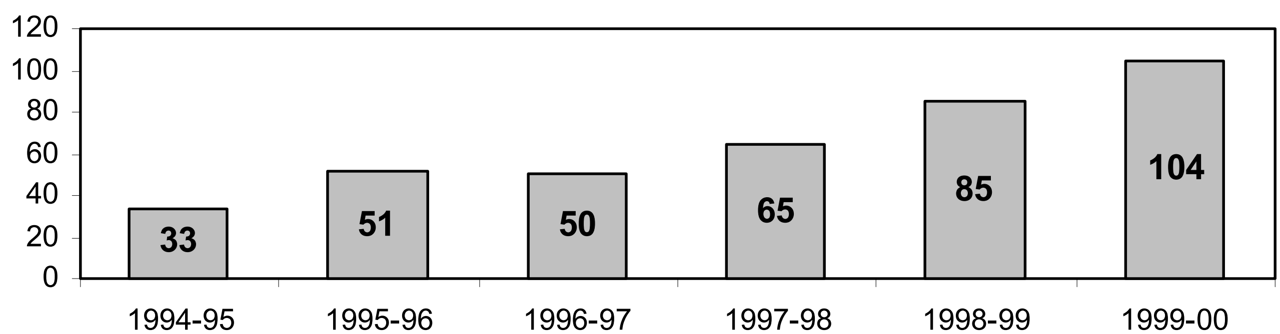
The issue is similar for PERS retirees who may wish to leave retirement to earn additional service credit. If their last employer was a school district or educational service district, and is now under SERS instead of PERS, the reitree would be unable to rescind their retirement and return to work for their last employer.

2. ***TRS 1 Post-retirement Employment***

The limits on post-retirement employment for TRS 1 members had been set at 75 days — approximately 42% of a school year. It was changed to an hourly measurement (525 hours) because in many instances substitutes and contract teachers in secondary schools do not teach an entire day, but rather may teach one or two classes per day.

In 1994, because of teacher shortages in many regions of the state, the legislature increased the number of hours on-call substitutes could work. School districts could submit resolutions declaring shortages of substitute teachers and many have done so (see Figure 2).

Figure 2
Substitute Teacher Resolutions by School Year



By submitting a resolution, school districts are allowed to increase the total hours a substitute teacher or principal can work to 840 -- to about 67% of the school year. In addition, they are allowed to increase the hours a substitute administrator or vice principal can work to 630 -- to about 50%

of the school year. But regardless of the increases in hours available for on-call substitutes, those working under contract are still limited to 525 hours.

There are 296 school districts in Washington State, so as of the 1999-2000 school year over one-third were filing shortage resolutions. This can be interpreted in a number of ways:

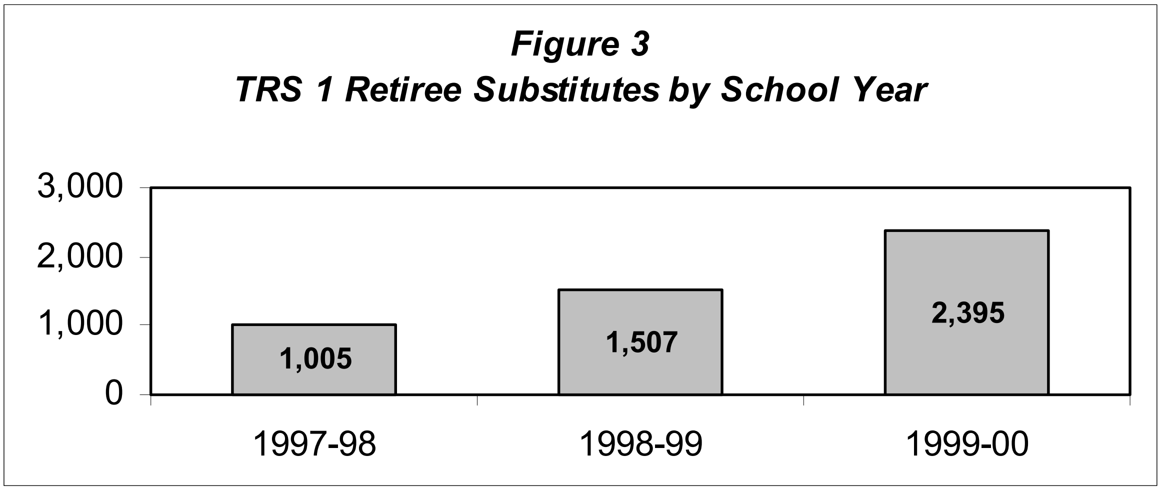
- The burgeoning economy may have enticed regular substitutes and other potential teachers (non-retirees) into better paying fields forcing school districts to turn increasingly to retirees to fill their substitute lists.
- It may be simply easier to recruit known entities (recent retirees) than screen new teacher candidates through the substitute lists.
- Increased use of leave benefits during the school year has boosted the total demand for substitutes, and retirees represent a readily available pool.

On-Call vs. Contract

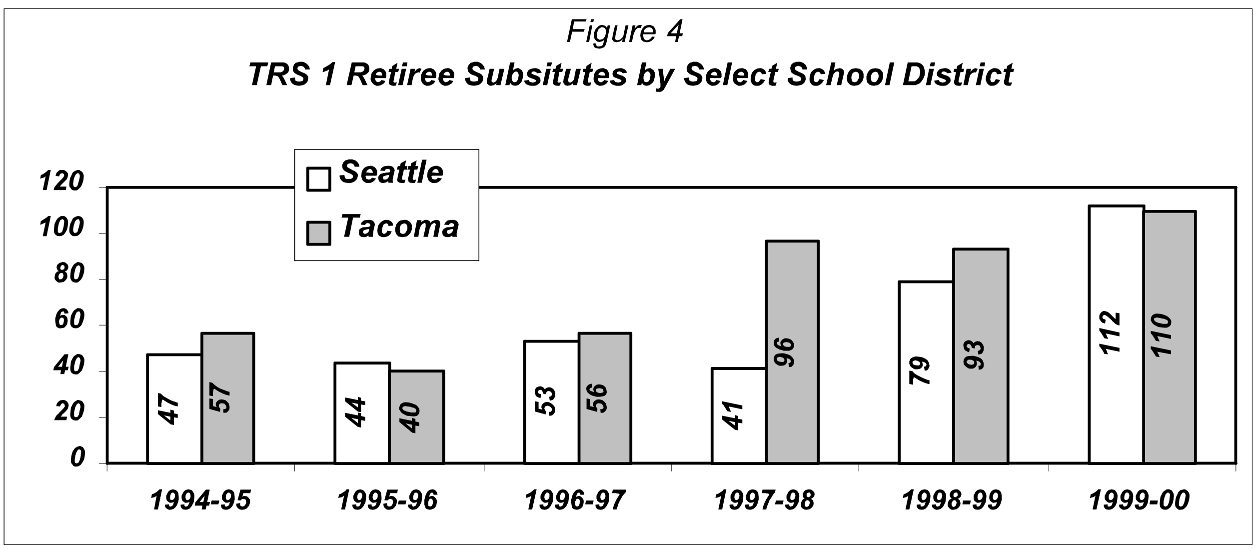
There is an important distinction between working **on-call** and working **under contract**. Substitutes in on-call situations are considered to be in informal employment relationships. The informality is characterized by the fact that they have no set work schedule. On-call substitutes are typically placed on a "substitute list" from which they are chosen when a regular teacher is gone; as a result, they may work several days a week or not at all. In contrast, those working under contract are engaged in what is considered "regular" employment, similar to active TRS 1 members. They have a formal employment relationship characterized by a set work schedule.

*3. **TRS 1 Retirees Working***

The number of TRS 1 retirees returning to work in teaching positions has grown significantly over the past several school years. During the 1997-1998 school year, just over 1,000 TRS 1 retirees were working as substitute teachers (see Figure 3). By the 1999-2000 school year that had over doubled to almost 2,400.



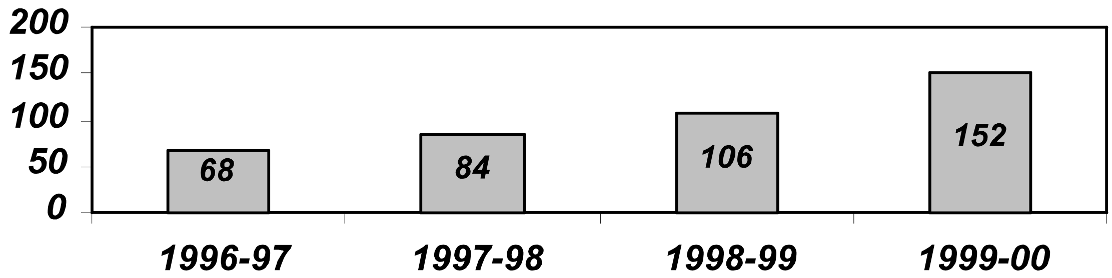
The shortage of substitutes has been felt similarly across the State but for different reasons. It would be expected that the larger metropolitan areas, though more desirable, would have difficulty attracting new teachers because of their higher cost of living (see Figure 4). And the smaller rural areas would continue to have difficulty because of their lack of amenities.



4. ***Benefits Suspended***

The increased use of retirees in on-call substitute and contract substitute positions is also seen in the number of retirement benefits that are suspended. This is, again, a very small number; the severity of the penalty for surpassing the hourly limit is such that it is relatively uncommon. Nonetheless, the number of suspensions has over doubled in the past three years (see Figure 5).

Figure 5
TRS 1 Pensions Suspended by School Year



5. ***Shifting Labor Markets***

An important factor that has likely given these issues their immediacy is the current labor market situation. In the last three calendar years, the unemployment rate in Washington State has been below 5%. Such a pattern of labor market tightness has not been experienced since the Korean War. Following the early 1950s the advent of such low unemployment has been an indicator of the peak of the business cycle. From the mid 1950s through the mid 1990s, the jobless rate in Washington had never attained such a low level for longer than one calendar year.

It was during the late 1960s through the early 1980s that the Baby-Boom generation entered the work force, thus creating an abundant supply of labor. It was also during this period that many more women joined the work force, further enhancing the labor supply. Contrast that with the more current situation where, as a result of a much lower birth-rates during the 1970s and 1980s, the availability of new entrants to the labor force has fallen markedly.

For these reasons, the current labor market situation may be considered endemic. No longer is the 5% unemployment rate an indicator of the business cycle peak, but rather is a result of significant demographic shifts. This is likely to drive equally significant changes in public and private human resource policies; policies that were established during the long period of labor abundance. Thus the playing field has changed form one in which employers had the advantage of abundant labor, to one in which new labor force participants have the advantage of their relative scarcity.

B. Prior Legislation

In an effort to assist those in the Plan 1 systems, the JCPP sponsored legislation that allowed PLAN 1 members to receive a refund of the contributions they made after 30 years of service. Members participating in this option would have their post-30-year contributions held in an interest-bearing account, and those moneys would be refunded to the member upon their retirement. Participants of the program earn 7.5% interest on their post 30-year contributions. Member's participating in this option have their benefits locked in based on earnings made at the time of participation. And members cease to accrue service credit after electing this option.

III. Proposals

A. Proposal to Modify the five month Limit on Post-retirement Employment

According to statute, PERS, SERS and TRS Plans 2/3 retirees are allowed to work 5 months per calendar year in an eligible position without loss of retirement benefits. At this time, those statutes have been interpreted very narrowly; if a retiree works a day in a given month, that month is debited from their 5-month allotment. This limits the kind of employment relationship in which a PERS, SERS and TRS Plans 2/3 retirees and employers may engage — short-term, full-time.

Contrast that with the method Department of Retirement Systems (DRS) uses to measure Teachers Retirement System Plan 1 member's post-retirement employment activity. A TRS 1 retiree may work 525 hours per year under contract or as an on-call substitute without the loss of benefits. Substitutes may even work longer (up to 840 hours) if a substitute teacher shortage resolution is filed by a school District with the DRS. Only when the retiree reaches or surpasses their allotted hours does the school district contact DRS. If the retiree has surpassed their allotted hours, the department will adjust or suspend their retirement benefit accordingly.

JCPP Recommendation:

It is the opinion of the Executive Committee that PERS, SERS and TRS Plans 2/3 retirees should be allowed to engage in employment relationships similar to that of TRS 1 retirees. As a result, The Executive Committee of the Joint Committee on Pension Policy recommends that PERS, SERS and TRS Plans 2/3 retirees be able to work up to 867 hours per calendar year without loss of retirement benefits.

Actuarial Impact: None.

B. Proposal to Increase the Allowable Hours of TRS 1 Retirees in Select On-Call and Contract Positions.

The limits on post-retirement employment for TRS 1 members originally had been set at 75 days, or approximately 40% of a school year, that a member could work without a reduction of pension. It was later changed to an hourly measurement (525 hours) because in many instances substitutes and contract teachers do not teach an entire day, but rather may teach one or two classes per day in secondary schools.

In 1994, because of teacher shortages in many regions of the state, the law was amended so as to allow retiree on-call substitute teachers, administrators, and principals to work a greater number of hours during the school year. School districts could submit resolutions to DRS declaring shortages of certified staff. In doing so they were allowed to increase the total hours an on-call substitute teacher or a substitute principal could work by 315 to a total of 840. Similar resolutions allowed school districts to increase the hours a substitute administrator or vice principal could work by 105 hours to a total of 630. But regardless of the increases in hours allowed for on-call substitutes, those working under contract were still limited to 525 hours.

JCPP Recommendation:

In recognition of teacher shortages in many school districts and in order to achieve greater consistency the Executive Committee of the Joint Committee on Pension Policy recommends that school districts be allowed to engage the services of TRS 1 retirees, either as on-call substitutes or under contract, using the same hourly allotments.

Substitute Positions	Existing Statute		Proposed Statute
	Standard	Additional with Shortages	Standard
On-call Teacher	525	315	840
On-call Administrator	525	105	840
On-call Vice Principal	525	105	840
On-call Principal	525	315	840
Under Contract	525	0	840

Actuarial Impact: None.

FISCAL NOTE

REQUEST NO.

RESPONDING AGENCY:	CODE:	DATE:	BILL NUMBER:
Office of the State Actuary	**035**	**11/3/00**	**Z-0273.1/01**

SUMMARY:

This bill impacts the Teachers' Retirement System (TRS) Plan 1 by increasing the number of hours from 525 to 840 a retiree can work without a suspension of their pension.

Effective Date: 90 days after session.

BACKGROUND DISCUSSION:

Under current provisions, only substitute teachers or administrators working for a district which has declared a shortage can work for up to 840 hours without a reduction in pension. The limit for substitutes in a district without a declared shortage, or those with a contract is 525 hours.

MEMBERS IMPACTED:

There are 296 school districts in the state of Washington. Districts must pass a resolution each school year to declare a shortage of qualified and available employees. The number of districts who have done so in the last three school years are:

	1997-98	1998-99	1999-00
Districts with shortage resolutions	65	85	104

Districts with separate resolutions for teachers and principals, etc. are counted only once in the above.

Substitutes in these districts will not be impacted.

Few substitute teachers work over the allowed hours in any event, and thus there will be no effect on most of their pensions.

There were 152 suspensions, mainly contract employees, in the 1999-00 school year. We do not have any data on how long they were suspended and what the effect of this bill would be on these individuals. This could mean an additional 2 to 4 months of benefits payable each year. The average monthly benefit in TRS 1 is $1,233. The average monthly benefit for a new retiree is $2,000.

Some employees may elect to retire earlier if they feel they can find work as a substitute or as part-time contract employee, after a month absence from work. This would be attractive since their pension and part-time salary could exceed their current salary. They may or may not continue to get medical benefits.

FISCAL IMPACT:

Actuarial Determinations:

In the short run this change has no effect on substitutes in those districts which would have declared a shortage, since the number of hours a retiree can work is the same. For districts which would not have declared a shortage the short term cost is likely to be small because few substitutes work long enough to require their pension to be reduced or suspended under the current provisions. There were 152 suspensions for employees working under contract in the 1999-00 school year. We do not have the data to determine the amount of the additional benefits which will be paid as a result of this provision.

In the longer run, active employees might elect to retire earlier knowing they could work 840 hours and receive a pension. This might be attractive since their pay and pension could exceed their full time pay. An employee deciding to do this would face the uncertainty of finding employment.

The cost to the system would equal:

1. Their annual pension;
2. Employer contributions;
3. Employee contributions;

offset by

4. Lower annual pension due to early commencement.

We could estimate these costs as follows:

1. The average benefit for a new retiree with 30 years of service is $24,000 a year.

2. Employer contributions are currently 7.10% of pay. If these contributions are no longer paid for a group of employees the rates will go up so that the amount of contributions are the same in total. The distributions of these amounts among the employers might change however.

3 & 4. These last two items offset each other for those with 30 years of service when pay increases are modest. The cost would be less if pay increases are more than a modest amount, or if those with less than 30 years of service elected to do this.

This would not generate an immediate increase in contribution rates, since the cost impact is not determinable without more information regarding how many active employees would take advantage of it and how much earlier they might retire. Rather the cost would emerge as a loss to the system as more participants retire than expected.

Fiscal Impact:

There is no increase in contribution rates and thus no increase in funding for the biennium.

State Actuary's Comments:

Some retirees will be able to teach up to 840 hours each school year and receive 100% of their retirement benefit. This may encourage many active teachers to retire and return to work to receive both their benefit and their salary. It is unclear to what extent this would take place.

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Gerald B. Allard, State Actuary

Uniform COLA at Age 66

Background:

PERS 1 and TRS 1 retirees are first eligible to receive Uniform COLA increases when they have both: attained age-66; and been retired one year. The determination of eligibility is made on July 1 of each year. As a result, retirees with birthdays after July 1st, do not become eligible to receive the COLA until the following year.

Committee Activity:

Presentation: Uniform COLA and Gain-sharing Status Report
May 25, 2000 Full Committee Meeting
Presentation:
October 18, 2000, Full Committee Meeting
Presentation:
November 15, 2000, Full Committee Meeting
Proposal Approved:
December 13, 2000, Full Committee Meeting

Recommendation to Legislature:

Amend Uniform COLA eligibility to include all retirees who have been retired one year and will have attained age-66 by December 31st in the year the benefit is paid.

Staff Contact:

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2000 Report on Cost-of-Living Adjustments (COLAs)

Joint Committee on Pension Policy

January 3, 2001

Prepared by:

Christine Masters Ryser

Research Analyst

Introduction:

This 2000 Report on Cost-of-Living Adjustments (COLAs) emphasizes the economic and demographic characteristics of Public Employees' (PERS) and Teachers' Retirement System (TRS) Plan 1 retirees and beneficiaries. It also provides information on gain sharing as it relates to both post-retirement increases for PERS/TRS 1 retirees and the Plan 3 counterpart -- gain-sharing payments to members' defined contribution accounts.

The goal of this report is to provide legislators and the public with a profile of current benefit recipients and to analyze the factors that determine who receives an increase and the size of that increase.

The source of the data used in this report is information collected and maintained by the Department of Retirement Systems. Unless indicated otherwise, all data is as of September 30, 2000.

Overview:

Cost-of-Living Adjustments:

The retirement plans administered by the state of Washington reflect a variety of approaches to providing cost-of-living adjustments (COLAs) to retirees. Differences exist in eligibility requirements and the level of income protection provided.

All current COLAs share common characteristics:

- ***Automatic:*** Not subject to legislative approval.
- ***Permanent:*** COLAs are ongoing features of the plans.
- ***Cumulative:*** Additional COLAs are added each year.
- ***Compounding:*** The amount of COLA rises each year. WSP is the only Washington system without an increasing COLA.

All plans developed since 1977 include the same 3% COLA design. COLAs for plans developed prior to 1977 differ substantially. The original designs range from LEOFF 1 with it's full CPI COLA to PERS/TRS 1 which provided only ad hoc COLAs. No two plans had identical cost-of-living provisions.

Table #1

Plan	Members Receiving	Description	Eligibility
PERS/ TRS 1	**40,054 19,563**	***Uniform/Minimum Benefit:*** A flat dollar amount per month per year of service which is increased each year by 3%.	• Age 66 or older and retired one year. • Age 65 or younger; and benefit less than the minimum benefit $28.33 per month per year of service, (as of 7/1/00.)
	26	***Age-65:*** Annual increase of up to 3%, based on an increase in the CPI.	When benefit received at age 65 has lost over 40% of its purchasing power.
LEOFF 1	**7,755**	Annual increase in CPI; compounding. No minimum benefit.	Retired one year.
WSP	**666**	***Retiree:*** Annual 2% simple increase; begins after member has been retired one year. Minimum benefit of $20 per month per year of service. ***Survivor:*** Receives Uniform COLA without gain-sharing component or; if member selects at retirement, a 2% simple increase.	Immediate at any age.
LEOFF/ PERS/ TRS/ SERS 2	**134 7,680 589 –**	Annual compounding increase of up to 3%; begins after member has been retired one year. No minimum benefit.	Retired one year.
TRS/ SERS 3	**142 –**	Defined benefit is increased same as Plan 2.	One year after begin receiving defined benefit payments.

When the Uniform COLA was enacted for PERS/TRS 1 in 1995, all previous COLAS for these systems were discontinued. A few members eligible for a higher benefit under the Age-65 benefit formula remained on that COLA. There were only 26 members receiving increases under the Age-65 COLA in 2000.

Gain-sharing:

In 1998, when gain-sharing was enacted for PERS/TRS 1 and Plan 3, a new mechanism for increasing benefits was created. Unlike the COLAs summarized in the table above, gain-sharing:

- Is contingent on the performance of retirement fund investments;
- Has no guarantee of continuation.

Gain-sharing is implemented differently in PERS/TRS 1 and Plans 3. In Plan 1, extraordinary gains boost increases in the Uniform COLA. Plan 3 extraordinary gains are distributed as a lump sum payment to eligible active and retired members' defined contribution accounts.

Characteristics of Benefit Recipients:

Former active members comprise the majority of people receiving public retirement benefits in all Plans. A small percent of recipients are the survivors or beneficiaries of the member. "Annuitants" refers to all benefit recipients, whether former members or their survivors.

Table #2

Summary of Annuitants

	PERS/TRS 1	LEOFF 1	WSP	Plans 2/3
Total Number	84,306	7,755	666	8,545
Average				
Current Age	72	63	63	69
Age at Retirement	60	51	53	65
Years of Service	22	22	28	12
Monthly Benefit	$1,144	$2,514	$2,506	$538
Monthly Benefit per YOS	$48	$134	$91	$45

Summary of COLA Payments:

The additional payments from all COLAs and gain-sharing in 2000 were more than $24 million over COLA payments made in 1999. Table 3 shows where additional benefits were generated based on data compiled for the 1999 valuation and 7/1/00 Uniform COLA calculation.

Table #3

2000 COLA Increases

System/Plan	Recipients	Payments
Plan 1		
PERS	40,333	$ 9,811,176
TRS	19,675	6,245,700
LEOFF	7,623	6,862,524
Plan 2		
PERS	6,765	1,176,300
TRS	398	104,016
LEOFF	100	28,476
Plan 3		
TRS	50	5,304
WSP[1]	647	37,344
(As of 12/31/99) **Total**	75,591	$ 24,606,960

Eligibility for Social Security Increases:

Almost all public employees are required to contribute to the federal Old Age, Survivors and Disability Insurance program – better known as Social Security. This benefit provides retirement benefits which increase at the same rate as the national Consumer Price Index (CPI). Adjustments are made each January. Retirees do not have to be retired for a certain amount of time before becoming eligible for this increase. In recent years, increases in Social Security were as follows:

Historical Increases to Social Security Benefits

1975-84	1985-94	1995	1996	1997	1998	1999
7.7%	3.5%	2.6%	2.9%	2.1%	1.3%	2.4%

Plan 1 COLAs:

Benefit Descriptions:

Retirees of PERS 1 and TRS 1 receive increases to their retirement benefits through the the Uniform COLA. Law Enforcement and Fire Fighters' Retirement System Plan 1 (LEOFF 1) members receive adjustments based on increases in the Seattle Consumer Price Index (CPI). The focus of this section is to provide information about PERS/TRS 1 COLA recipients and non-recipients. Information about LEOFF 1 benefit increases is included at the end of this section.

- ***Uniform COLA***

  To be eligible for this annual adjustment, retirees must satisfy one of two criteria:

  - Be age-66 or older and retired for at least one year by July 1; or
  - Receive a benefit that is below the minimum threshold.

  The adjustment, known as the "annual increase," is based on a flat amount per month per year of service. The annual increase for July 1, 2000 was $1.08. At this amount, an eligible retiree with 30 years of service would have received an increase of $32.40 per month starting July 1st. (30 x $1.08 = $32.40.)

  The annual increase itself increases each year by 3%. The annual increase on July 1, 2001 will be $1.11. ($1.08 x 1.03 = $1.11.)

  The Uniform COLA may be further increased by a gain-sharing distribution in even-numbered years. Gain-sharing increases become a permanent part of the base Uniform COLA amount used to calculate future 3% increases. Graph #4 on page 10 illustrates this process.

- ***Minimum Benefit COLA***

  Retirees younger than age 66 may receive the Uniform COLA if their benefit falls below the minimum benefit threshold. The minimum benefit acts as a threshold or trigger for eligibility to receive the Uniform COLA.

  The minimum benefit threshold is increased each July 1 by the same annual increase amount determined for the Uniform COLA. On July 1, 2000 the minimum benefit threshold was $28.33. It will increase by $1.11 to $29.44 on July 2001.

  Retirees who are above the minimum threshold may become eligible for the Uniform COLA in the future if the minimum increases beyond their benefit.

- ***Gain-sharing***

  Plan 1 gain-sharing is a biennial process that increases the amount of the Uniform COLA when "extraordinary gains" occur. “Extraordinary gains” is a term defined in statute. It occurs when the rate of return (ROR) on PERS/TRS 1 retirement fund investments for the previous two bienniums, (4 years) averages over 10%. The amount of each gain-sharing increase is dependent on the amount of extraordinary gains.

  The gain-sharing amount is determined in even-numbered years by applying the ROR in excess of 10%, to half the assets held on July 1st of that year. Gain-sharing distributions are made in odd-numbered years. Half of the gain-sharing amount is used to provide a permanent increase in the Uniform COLA. The other half is used to shorten the amortization period for the PERS/TRS 1 unfunded liability.

  All members, active and retired, realize the benefits of gain-sharing, but not simultaneously. Retired members receive an immediate increase in the Uniform COLA amount when gains are calculated. Active members realize gain-sharing benefits after retirement. At this time they become eligible for a COLA amount which has been increased by past gains.

  Extraordinary gains are not something that will occur on a regular basis or in predictable amounts. This process will produce highly erratic results from biennium to biennium. It is likely there will be long periods of time when no extraordinary gains occur. When they do occur, they may be very small or very substantial.

  This highly erratic process is used to provide additional increases to the Uniform COLA–a very regular and stable process.

Calculation of the 2000 Plan 1 Gain-sharing Uniform COLA Increase:

Rates of Return				
Fiscal Year				4-year
1996	**1997**	**1998**	**1999**	**Average**
17.4%	20.5%	16.6%	11.9%	16.56%

16.56% - 10% = 6.56%

Half of the combined PERS/TRS 1 assets are multiplied by 6.56%. This produces the Plan 1 extraordinary gain.

50% of PERS/TRS 1 assets =	$9,668 M
$9,668M x 6.56% (gain-sharing percent) =	$634 M (extraordinary gain)

The state actuary calculates how much of a permanent increase to the Uniform COLA can be funded with $634M. In future years, the Uniform COLA's annual 3% increase is applied to the total COLA amount, including any increases attributed to gain-sharing.

The gain sharing increase to the Uniform COLA was $0.28 effective January 1, 2000. When added to the Uniform COLA amount of $0.77, retirees' benefits were increased a total of $1.05 per month per year of service.

This COLA amount was in effect from January until July 1, 2000. In July the COLA was increased by 3% of $1.05 to $1.08. The Uniform COLA will remain at this amount until adjusted again in July 2001.

COLA Policy for PERS/TRS 1:

Eligibility for a COLA in PERS/TRS 1 is shaped by policies implicitly and explicitly adopted by the Legislature.

The age-66 trigger for eligibility is significant for several reasons:

- It is the age when members of the Plan 2/3 systems are first eligible to retire and, after one year, (when they are 66), begin receiving the 3% COLA. The benefit provided to Plan 1 members does not start earlier than that provided to Plan 2/3 members.

- It approximates the age requirement for full Social Security benefits.

- It is considered the age when workers were most likely to permanently leave the workforce. At this point they lose the ability to replace losses in purchasing power with employment income.

In almost all of Washington's public plans COLA increases are based on a percent of benefit. The amount of the retiree's monthly benefit is multiplied by a percentage, and increases compound from year to year. This approach provides more dollars to those retirees with larger benefits. The Uniform COLA is distributed based on the member's years of service. This approach distributes the largest increases to those members who have provided the longest service.

Demographics of Plan 1 Retirees:

Of the 84,306 annuitants receiving retirement benefits in PERS/TRS 1, fully 70% receive an annual cost-of-living increase. Increases for individual members were calculated on an average of 19 years of service in PERS 1 and 24 years in TRS 1. Based on the July 1, 2000 Uniform COLA amount of $1.08, the average Plan 1 member saw an increase between $20.52 and $25.92 per month.

Table #4

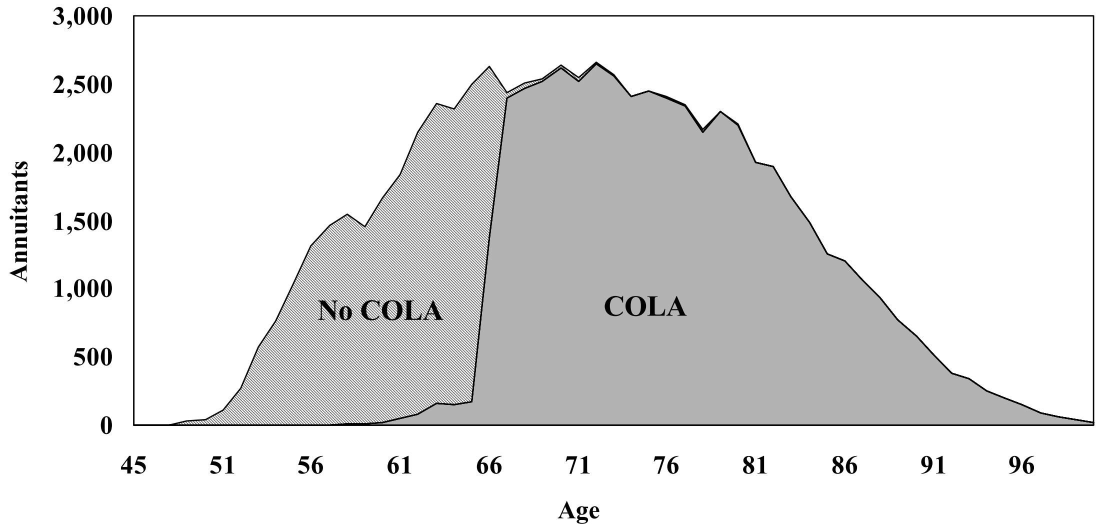
Summary of PERS/TRS 1 Annuitants

	Receiving Uniform/Minimum		Not Receiving Uniform/Minimum	
	PERS 1	**TRS 1**	**PERS 1**	**TRS 1**
Total number	40,054	19,563	13,161	11,528
Average				
Current Age	77	77	60	60
Age at Retirement	63	61	56	56
Year of Retirement	1985	1984	1996	1996
Years of Service	19	24	25	28
Monthly Benefit	$793	$1,087	$1,742	$1,777
Monthly Benefit Per Year of Service	$40	$44	$66	$64

Graph #1

PERS/TRS Plan 1

COLA Status by Age

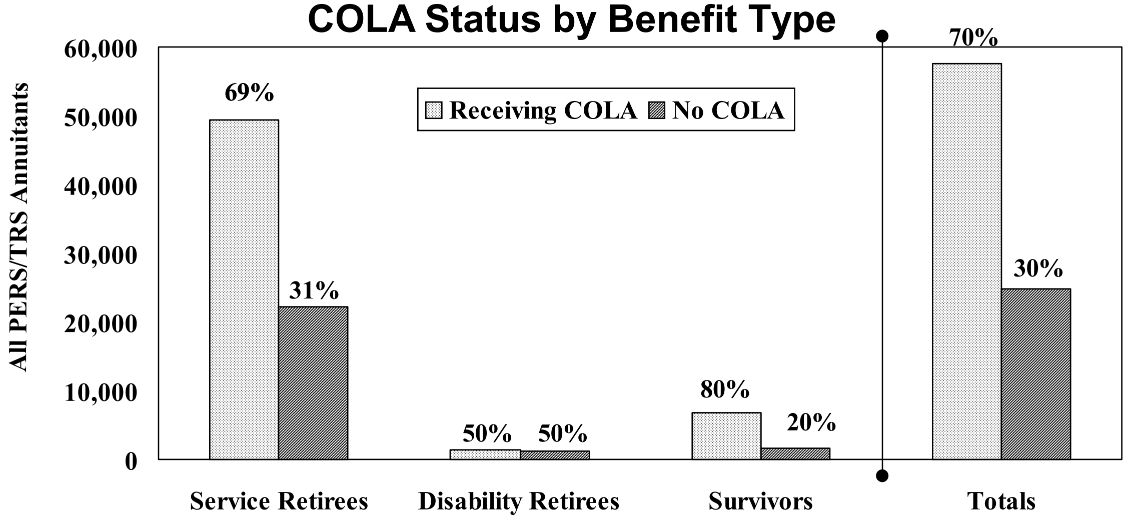


Whether an annuitant receives a COLA is largely a function of age. Almost all annuitants will eventually qualify for the Uniform COLA. Members born before July 1 and retired for at least one year, begin receiving the Uniform COLA the year they turn age-66. Members born after July 1, begin receiving the COLA the following July 1 when they are between the ages of 66.5 and 67.

Graph #2

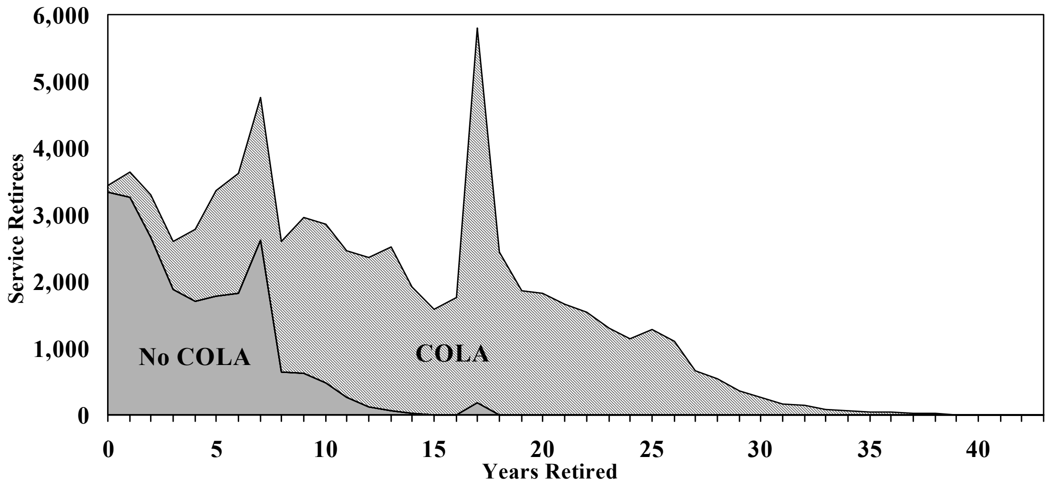
PERS/TRS Plan 1

COLA Status by Benefit Type



Annuitants qualify for benefits under three scenarios. Most often, they are service retirees, members who have met the age and/or years of service requirements to begin receiving benefits. In other cases, they qualify as disability retirees or as the designated survivor of a retiree. Graph 2 shows the number of annuitants receiving or not receiving a Plan 1 COLA according to these three categories.

Graph #3
PERS/TRS Plan 1
COLA Status by Years Retired



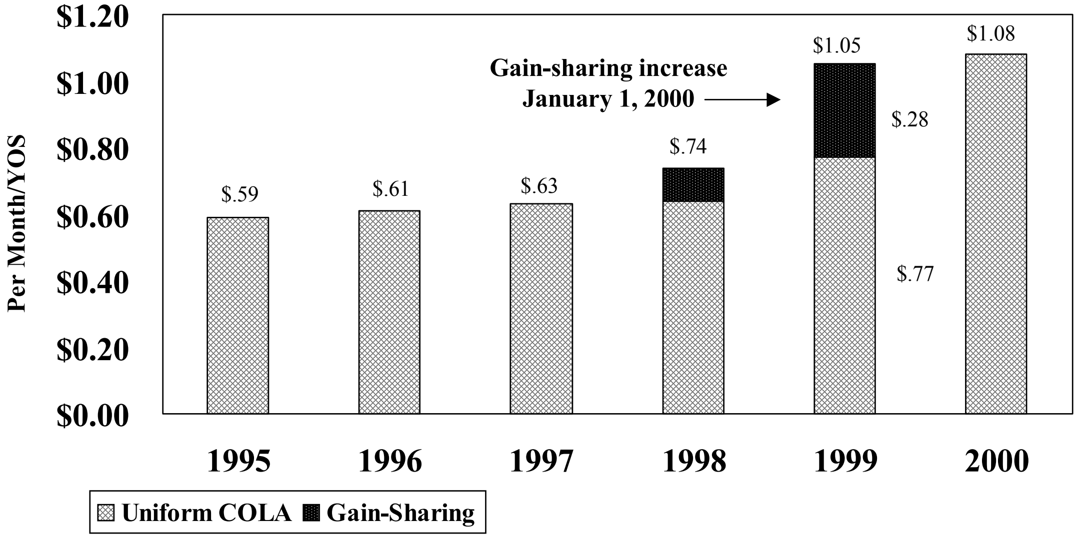
Graph 3 displays the numbers of service retirees receiving and not receiving a COLA according to how long the retiree has been retired.

Spikes in the graph are the results of early retirement windows offered in previous years. During those periods, unusually large numbers of members retired, some at relatively young ages. Some of these members have yet to reach COLA eligibility (age-66), even after several years of retirement.

The Value of the Uniform COLA:

The value of the Uniform COLA increases each year by 3%. In even-numbered years gain-sharing may boost the COLA further. Graph #4 shows the growth of the Uniform COLA since inception and the effect the two gain-sharing distributions have had on the current level of the COLA.

Graph #4
PERS/TRS Plan 1
Uniform COLA Increase



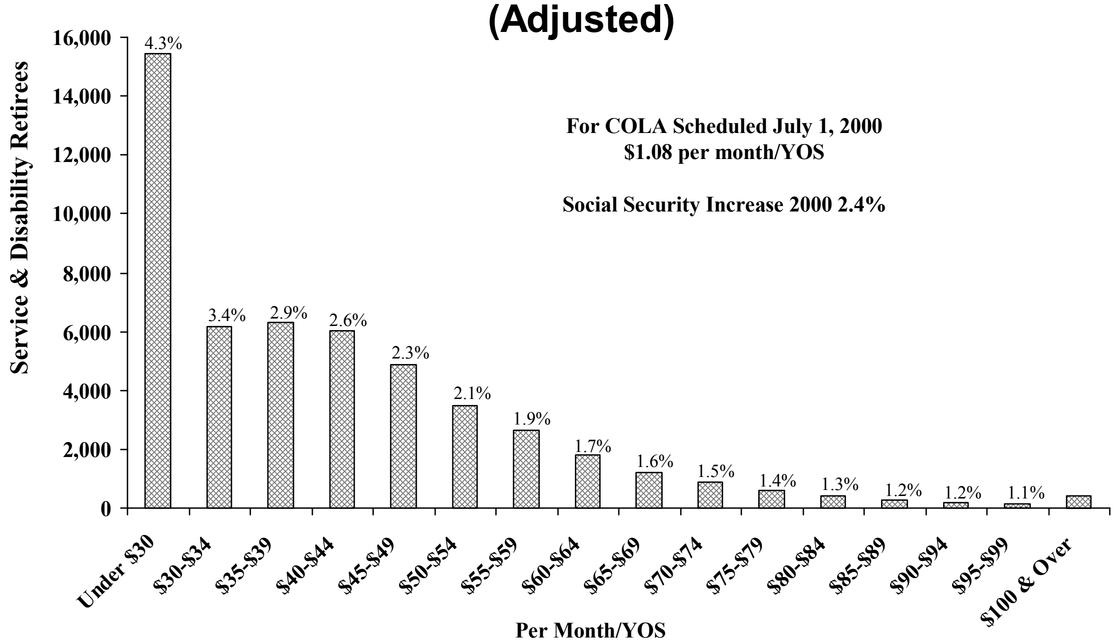
Retirement benefits are based on the number of years of service and the average final salary the member earned before retirement. When looking at a member's benefit that is small it is impossible to tell whether it is small because the member had very little service credit, a low salary, or both. It is more informative to look at a retiree's benefit on a per year of service basis. For example, if a retiree receives $800 per month and had 20 years of service, then the retiree receives $40 per month for each of their 20 years ($800 ÷ 20 = $40 per month/YOS).

Retirees with a low benefit per year of service must have had a low salary. This could be caused by one or more of the following. The:

- Benefit was calculated using a salary from many years ago;
- Member had a low paying job; or
- Member worked part-time but received full service credit. A part-time salary with full service credit produces a benefit that is indistinguishable from a full-time person who makes a low salary.

Comparing the Uniform COLA to COLAs that provide a percentage increase is difficult. It requires that we calculate the percentage increase in the $/month/YOS each member receives under the Uniform COLA formula. Someone who receives $40 per month/YOS and receives the Uniform COLA increase of $1.08 per month/YOS, recognizes a 2.70% increase in their benefit; ($1.08 / $40.00 = 2.70%). Retirees with higher or lower benefits per month/YOS will recognize differing percentage increases.

Graph #5
PERS/TRS Plan 1
Uniform COLA Percentage Increase (Adjusted)



Graph #5 demonstrates the range of percentage increases provided by the July 2000 Uniform COLA. Benefits shown have been adjusted to remove the impact of TRS annuity withdrawals and benefit payments that include survivor options.

The Uniform COLA increase distributed July 1, 2000 was $1.08 per month/YOS. For retirees who receive a benefit less than $30 per month/year of service, this amounted to a 4.3% increase in benefits. Retirees at the other end of the graph, who were receiving benefits of $95 to $99 per month/YOS saw an increase of only 1.1% in their benefits.

As a comparison, Social Security (SS) benefits increase each year by the full increase in the national Consumer Price Index (CPI). In 1999, SS benefits increased by 2.4% for all retirees. LEOFF 1 benefits are increased by changes in the CPI for Seattle. In 1999 benefits for LEOFF 1 retirees increased by 3.1%.

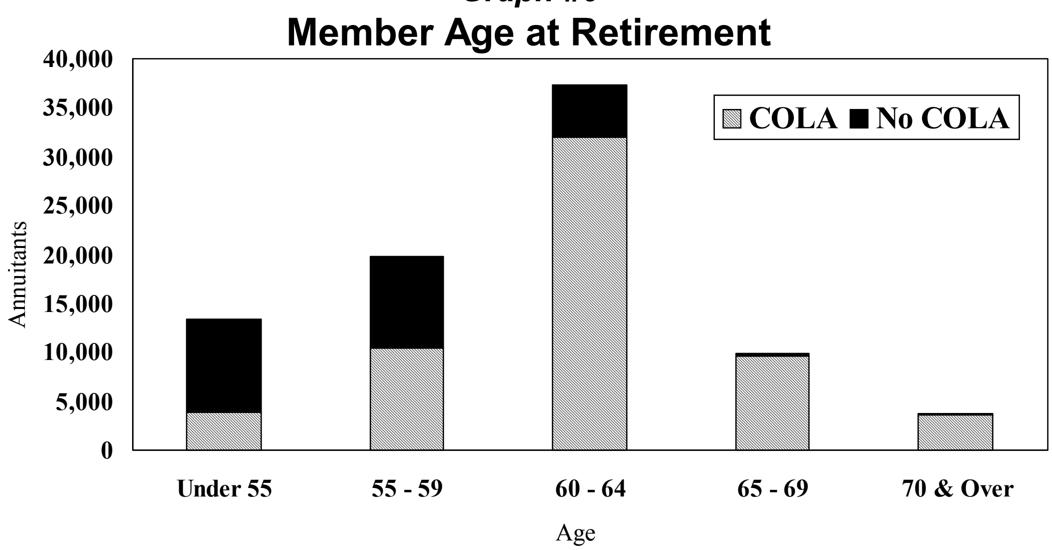
Characteristics of Plan 1 Retirees and Benefits:

As with any group of 84,000 individuals, there are both differences and similarities among its members. In understanding the impact of the Uniform COLA on PERS/TRS 1 benefits, the following variables are most useful.

Age at Retirement:

Members who retired before age-65 are less likely to be currently receiving a COLA. This is attributed to the age-66 requirement for COLA eligibility. By far, the majority of members leave employment between the ages of 60 and 65.

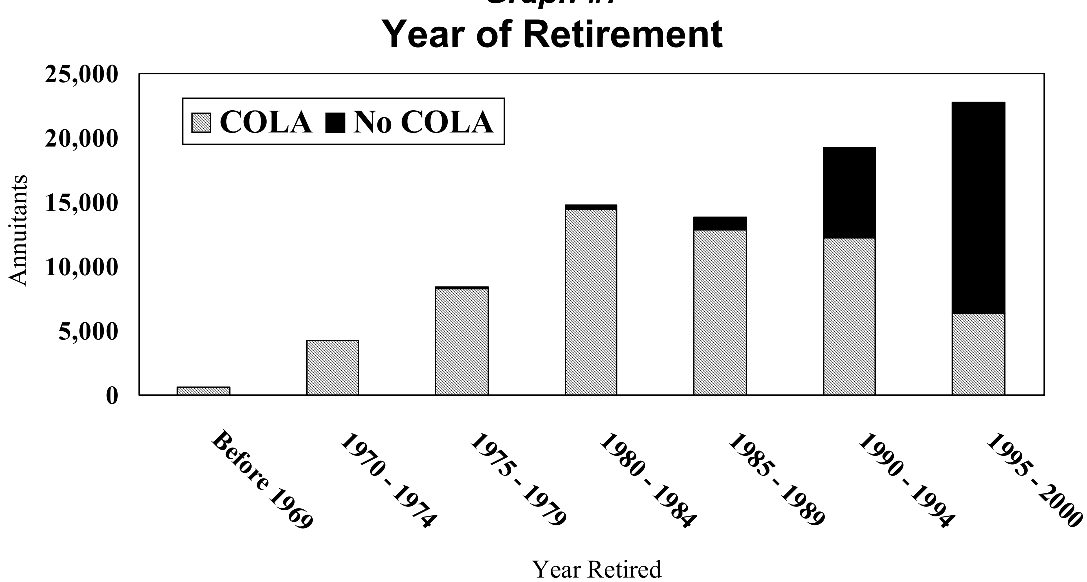
Graph #6



Year of Retirement:

The relatively early retirement provided in Plan 1 (any age with 30 YOS; 55 with 25 YOS; and age-60 with 5 YOS) means that many retirees will not qualify for a COLA in their first years of retirement. Members who have been retired the longest are most likely to be receiving a COLA. Annuitants with retirement dates prior to 1985 and still not receiving a COLA are primarily beneficiaries who have not yet attained age-66.

Graph #7

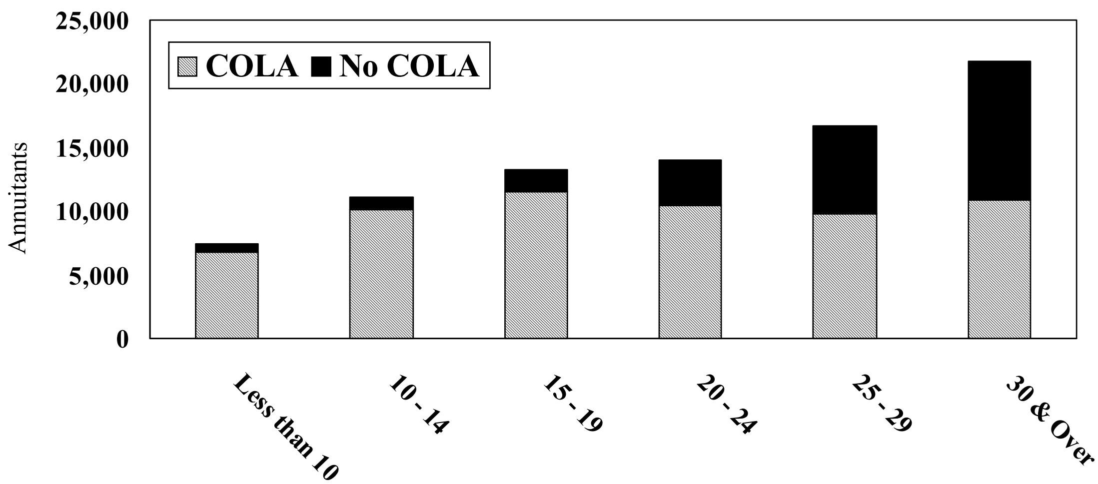


Years of Service:

PERS/TRS 1 retirement eligibility provisions allow members to retire as many as 10 years before they become eligible for a COLA. Members with over 30 years of service are eligible to retire at much younger ages. Shorter-service retirees show a higher percentage of COLA eligibility. Usually they joined the Plan at higher ages and qualified for retirement by attaining age-60 with at least 5 years of service. These members are within 6 years of COLA eligibility.

Graph #8

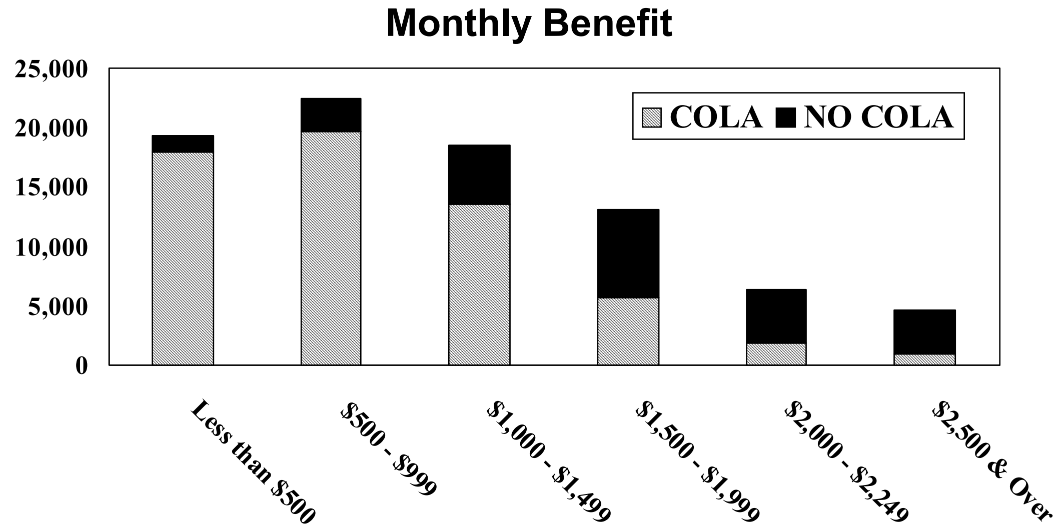
Years of Service



Monthly Benefit:

The distribution of monthly benefits shows a larger percentage of retirees with lower benefits receiving the COLA. This trend is influenced by two factors. Lower monthly benefits generally indicate low service or are based on salaries earned many years ago. Retirees with smaller monthly benefits are more likely to be older and thus eligible for COLA increases. Larger benefits are more likely to represent recent retirement and longer service. More recent retirees and those who retire under service eligibility tend to be younger. A smaller percent of these retirees are currently receiving COLAs.

Graph #9



PERS/TRS 1 Minimum Benefit Recipients:

Minimum benefit recipients form a relatively small sub-group of retirees receiving an annual increase. Out of approximately 59,617 retirees receiving COLAs, only 1,103 (less than 2%) do so under minimum benefit eligibility.

Currently, a monthly salary of $1,415 will produce a benefit qualifying the retiree for the minimum benefit. Salary level alone is not the only factor contributing to eligibility. In most cases it is low pay, coupled with full-time service credit.

Full-time service credit is earned with 70 hours a month for PERS 1 members. This is about 40% of full time. TRS 1 members earn 12 months of credit for 144 days of service during a school year (September-August). Under these provisions, members who are engaged in part-time employment often qualify for full-time service credit. Meanwhile the salaries used in calculating their benefits reflect less-than full-time earnings.

The result is a low benefit per year of service. A Plan 1 member who works 40% of full-time in a position with a monthly salary of $3,540, earns $1,415 per month. At 40% of full-time, they will still earn full service credit. This produces a benefit per month/YOS of $28.33 – the current minimum benefit threshold.

Table #5

Summary of Minimum Benefit Recipients	PERS 1	TRS 1
Total Number	919	184
Average		
Current Age	62	62
Age at Retirement	55	54
Year of Retirement	1993	1992
Years of Service	17	12
Monthly Benefit	$ 432	$ 283
Monthly Benefit Per Year of Service	$ 25	$ 24

LEOFF 1 COLA:

All LEOFF 1 retirees begin receiving a COLA after they have been retired for one year. In the first year they are eligible for the COLA, they also receive a retroactive increase for the first year of retirement. COLA amounts are equal to the full rise/fall in the Seattle CPI. Benefit adjustments are made April 1 of each year.

LEOFF 1 retirees and eligible spouses receive the same retirement benefits and post-retirement increases. Table 6 shows averages for all annuitants.

Table #6

Summary of LEOFF 1 Annuitants	
Total Number	7,755
Average	
Current Age	63
Age at Retirement	51
Years of Service	22
Monthly Benefit	$2,514
Monthly Benefit Per Year of Service	$134

Table #7

Basis for LEOFF 1 COLAs
Urban Wage Earners and Clerical Workers, Seattle, WA, All Items, Series A

Year	Increase	Year	Increase	Year	Increase
1985	2.08%	**1990**	7.11%	**1995**	2.90%
1986	0.71%	**1991**	5.53%	**1996**	3.30%
1987	2.35%	**1992**	3.54%	**1997**	3.10%
1988	3.30%	**1993**	2.98%	**1998**	2.63%
1989	4.68%	**1994**	3.66%	**1999**	3.10%
5-Year Avg.	2.62%		4.56%		3.00%

Plan 2/3 Defined Benefit COLA:

The Plan 2/3 COLA is similar to the LEOFF 1 COLA in that each retiree is entitled to the full CPI increase from retirement. The difference is that Plan 2/3 retirees can never get an increase that is greater than 3% of the previous year's benefit. The CPI has almost always been greater than 3% and therefore, all Plan 2/3 retirees have received 3% COLAs in most years.

The size of each Plan 2/3 retiree's COLA is determined by the total amount of change in the CPI since the year they retired. Retirees of different years can receive a different COLA amount depending on the total increase in the CPI since their retirement. There is also the possibility Plan 2/3 retirees could get an increase when the CPI is negative. This would happen when the total increase in the CPI has averaged more than 3% per year since retirement.

Plan 2/3 retirees receive a COLA on the first July 1st after they have been retired one year. Plan 2/3 survivors receive the same COLA as retired members.

Plan 2/3 members need to be age-65 to receive unreduced benefits. If they retire prior to age-65 they must take an actuarially reduced benefit. The calculation of the actuarially reduced benefit includes a reduction for beginning the COLA earlier than age-66.

Plan 2 members are considered retired when they begin receiving monthly benefits. In Plan 3, a member is not considered retired for COLA purposes until they begin receiving monthly benefits from the defined benefit portion of their benefits.

Table #8

Summary of Plan 2/3 Annuitants	Plan 2			Plan 3
	LEOFF	PERS	TRS	TRS
Total Number	134	7,680	589	142
Average				
Current Age	61	69	67	60
Age at Retirement	58	65	64	59
Years of Service	12	11	13	15
Monthly Benefit	$ 885	$ 514	$ 812	$ 346
Monthly Benefit Per YOS	$ 75	$ 44	$ 63	$ 23

TRS Plan 3 Gain-sharing Distributions:

Plan 3 benefits include a gain-sharing mechanism very similar to the one administered for PERS/TRS 1 retired members. The primary differences are:

- Plan 3 gain-sharing is distributed in the form of a lump sum deposited into members' defined contribution accounts.
- Plan 3 extraordinary gains are not specifically designed as cost-of-living adjustments as they are in Plan 1. They do serve the same function of increasing the overall value of benefits.
- Retirees and actives receive the benefit of extraordinary gains at the same time.

The amount of each gain-sharing distribution is dependent on the rate of return (ROR) on defined benefit investments of plan 2/3. When the ROR for the previous two biennium averages over 10%, half of the amount over 10% is used to provide a lump sum payment to active and retired members.

The first TRS 3 gain-sharing payments were made in 1998. A second one occurred in 2000. In the future two new plans, SERS 3 and PERS 3 will also be part of the gain-sharing calculation. A gain share is calculated using all Plan 3 service earned to date. Individual members receive payments based on the gain share, multiplied by their years of service. Gain-sharing is calculated and distributed to members' defined contribution accounts in January of even-numbered years (once each biennium.)

Calculation of the 2000 Plan 3 Gain-sharing Distribution:

Rates of return were as follows for the 4 years between 1996 and 2000:

Rates of Return

1996	**1997**	**1998**	**1999**	**4-Year Average**
17.4%	20.5%	16.6%	11.9%	= 16.56%

16.56% - 10% = 6.56%

Half of the combined Plan 3 assets are multiplied by 6.56%. This produces the amount of extraordinary gains available for distribution to members in 2000.

50% of PERS 2 and TRS 2/3 assets =	$6,997 M
$6,997 M x 6.56% (gain-sharing percent) =	$459 M
Percentage of total Plan 2/3 service credit in Plan 3=	15.88%
$458 M x 15.88% =	$72.9 M (distributed)
$72.9 M ÷ 286,702 (years of Plan 3 service) =	**$254.23** per YOS

Table #9

TRS 3 Gain-sharing
Historical Summary

Year	Eligible Members	Average Years of Service	Total Dollars Distributed *(In Millions)*	Gain-sharing	Average Dollars to Members
1998	27,243	7.8	$28.4	$134.43	$1,042
2000	35,529	8.1	$72.9	$254.23	$2,051
Total			**$101.3**		**$3,093**

Table #10

TRS 3 Gain-sharing 2000 Distribution						
		Total			Average	
		Years of	Dollars Distributed	Years of	Dollars to
Eligible Members		**Number**	**Service**	*(In Millions)*	**Service**	**Member**
Active		34,749	278,641	$71	8.0	$2,039
Retired		225	2,590	$1	11.5	$2,926
Term-Vested		555	5,471	$1	9.9	$2,507
	Total	**35,529**	**286,702**	**$73**	**8.1**	**$2,051**
Ineligible Members						
Not Vested		2,257	3,474		1.5	
DC Account Balance Less Than $1,000		3,397	1,033		0.3	
	Total	**5,654**	**4,508**		**0.8**	

A small segment (14%) of all Plan 3 members were ineligible for the 2000 gain-sharing distribution. These members did not have $1,000 in their account balance and were not vested or did not earn service credit during the year.

Washington State Patrol:

WSP COLA Policy:

WSP is the only publicly funded system which differentiates between retiree and survivor benefits. Retirees receive a benefit based on their years of service. This base benefit is increased each year by a simple 2% non-compounding COLA.

Survivors receive a benefit which is half of the member's average final salary. They are not eligible for COLAs until age-66, when they begin receiving the WSP Uniform COLA increase. The WSP Uniform COLA increase amount is similar to the PERS/TRS 1 Uniform COLA amount except that it does not include any increases based on gain-sharing.

Under original provisions, WSP benefits were not reduced to provide on-going benefits to the retiree's beneficiary. WSP is the only public plan with this feature that is currently accepting new members. In 1999, the Legislature acted to provide a second benefit payment option in the WSP system. Retirees after July 1, 2000 may elect to receive an actuarially reduced benefit in exchange for continuing their full benefit to their survivor. The new benefit payment option includes an annual 2% simple COLA for the survivor.

Annuitant Demographics:

The difference in benefit levels for retirees and survivors creates two separate annuitant groups.

Table #11

WSP Annuitant Summary Statistics
(As of 12/99)

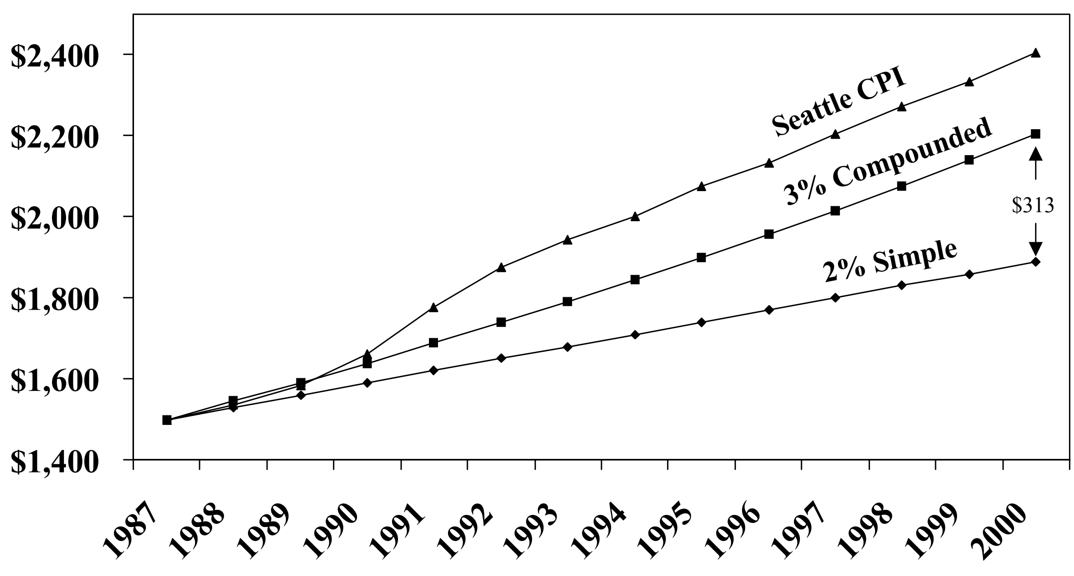
	Retirees	Survivors
Total Number	537	110
Percent of Annuitants	83%	17%
Average		
Age	61.2	71.8
Years of Service	28.8	11.7
Monthly Benefit	$2,694	$994

The following graph illustrates the increases produced under the current 2% simple COLA design and the 3% compounding design applied in all other Washington systems currently open to new members. The graph is based on a initial benefit of $1,500 per month.

The retirement allowance of those receiving a simple 2% annual cost-of-living adjustment would have increased from $1,500 to $1,890 between 1987 and 2000, a gain of 26%. The allowance of those receiving a compounding 3% COLA would have increased from $1,500 to $2,203. This is a gain of 46.9%. By 2000, the difference in monthly benefits produced by the two formulas would be $313 or 16.6%.

Graph #10

Growth of Retiree Benefits Chart



Committee Recommendations:

Plan 1 Uniform COLA Eligibility

Currently a retired member of PERS 1 is first eligible to receive the Uniform COLA when they have been retired for one year and have attained age-66 by July 1st. As a result, retirees who have been retired one year, but do not reach age-66 until after July 1, must wait until the next July 1st to begin receiving the Uniform COLA.

The JCPP recommends an adjustment in the age requirement for Uniform COLA eligibility. Retirees who have been retired for one year by July 1st will begin to receive the COLA on July 1st if they will reach age-66 during the calendar year.

This proposal has no impact on those already receiving the Uniform COLA or on those born in January through June. Those born July through December will begin to receive the Uniform COLA a year earlier. (See Fiscal Note in Appendix A.)

WSP Cost-of-living Adjustment Increase:

Washington State Patrol (WSP) retirees now receive a 2% non-compounding increase on benefits. Their survivors receive increases according to one of two mechanisms:

1. Survivors of retirees retired before July 1, 1999 receive Uniform COLA increases when they reach age-66 eligibility.

2. Members who retire after July 1, 1999 may choose a benefit payment option that continues the member's full benefit on to a survivor and includes a simple 2% non-compounding COLA. Retirees who select this option receive an actuarially reduced benefit.

The JCPP recommends the annual 2% simple COLA for WSP retirees and survivors be increased to a 3% compounding formula beginning in July 1, 2001. (See Fiscal Note in Appendix B.)

Appendix A

FISCAL NOTE

REQUEST NO.

RESPONDING AGENCY:	CODE:	DATE:	BILL NUMBER:
Office of the State Actuary	**035**	**10/24/00**	**Z-0224.5/01**

SUMMARY:

This bill impacts the Public Employees' Retirement System (PERS) Plan 1 and Teachers' Retirement System (TRS) Plan 1 by allowing those who have been retired for one year, and will be at least age 66 by December 31st, to receive the annual increase paid on July 1st of that year.

Effective Date: July 1, 2001.

BACKGROUND DISCUSSION:

The current provision requires the member to have been retired one year and to be at least age 66 on July 1st to eligible for the annual increase paid that year. This means that some members will get their first COLA as early as age 66, while others will not get theirs until age 67 (or one to two years after retirement if later). This bill would change this so that some members would get their COLA as early as age 65½, while others will not get theirs until age 66½ (or one to two years after retirement if later).

MEMBERS IMPACTED:

We estimate that 50% of the members who are under age 65 would be affected by this bill.

TRS Plan 1	Under Age 65	Total
Receiving a Benefit	8,196	28,920
Actives	18,525	18,737
Vested Terminated	2,071*	2,071

PERS Plan 1	Under Age 65	Total
Receiving a Benefit	10,446	52,515
Actives	27,390	28,168
Vested Terminated	3,295*	3,295

******All are assumed to be under age 65.*

We estimate that for a typical member impacted by this bill, the annual increase would be paid one year earlier. The annual increase for July 1, 2001 in the monthly benefit is $1.11 times years of service. The annual increase is increased by 3% each year and by future "gain-sharing" amounts. The typical recipient of the Uniform COLA has 19 years of service in PERS and 25 years of service in TRS.

FISCAL IMPACT:

Actuarial Determinations:

The bill will impact the actuarial funding of the system by increasing the present value of benefits payable under the System and the required actuarial contribution rate as shown below:

Teachers' Retirement System and Public Employees' Retirement System (Plan 1):

(Dollars in Millions)	**System:**	**Current**	**Increase**	**Total**
Actuarial Present Value of Projected Benefits The Value of the Total Commitment to all Current Members	PERS 1 TRS 1	$12,494 10,382	$ 36 32	$ 12,530 10,414
Unfunded Actuarial Accrued Liability The Portion of the Plan 1 Liability that is Amortized until 2016	PERS 1 TRS 1	$ 1,589 1,263	$ 36 32	$ 1,625 1,295
Unfunded Liability (PBO) The Value of the Total Commitment to all Current Members Attributable to Past Service	PERS 1 TRS 1	$ 809 663	$ 32 28	$ 841 691
Required Contribution Rate-Employer/State	PERS TRS	3.21% 5.38%	.04% .09%	3.25% 5.47%

Fiscal Budget Determinations:

As a result of the higher required contribution rate, the increase in funding expenditures is projected to be:

	PERS/SERS	**TRS**
Increase in Contribution Rates:		
Effective 9/1/2001		
Employee (Plan 2)	0.00%	0.00%
Employer	0.04%	0.08%

	PERS/SERS	TRS
Costs **(in Millions)**:		
2001-2003		
State:		
General Fund	$ 1.4	$ 4.1
Non-General Fund	1.6	0.0
Total State	**$ 3.0**	**$ 4.1**
Local Government	$ 2.7	$ 0.9
2001-2005		
State:		
General Fund	$ 3.0	$ 8.7
Non-General Fund	3.5	0.0
Total State	**$ 6.5**	**$ 8.7**
Local Government	$ 5.9	$ 2.0
2001-2017		
State:		
General Fund	$ 16.5	$ 46.3
Non-General Fund	19.1	0.0
Total State	**$ 35.6**	**$ 46.3**
Local Government	$ 32.7	$ 10.5

Gerald B. Allard, State Actuary

Appendix B

FISCAL NOTE

REQUEST NO.

RESPONDING AGENCY:	CODE:	DATE:	BILL NUMBER:
Office of the State Actuary	**035**	**12/6/00**	**WSP Draft**

SUMMARY:

This bill impacts the Washington State Patrol Retirement System by:

1. Changing the COLA from a simple 2% to a 3% CPI-based adjustment for beneficiaries as well as retirees.

2. Changing the employee contribution rate from a fixed 7% to the greater of 2% or the employer rate.

3. Excluding prospectively voluntary overtime from the definition of salary.

and in addition for members commissioned after January 1, 2003 by:

1. Changing from a 2 year to a 5 year Average Final Salary.

2. Excluding annual and holiday pay cash-outs.

3. Changing military service to include only up to 5 years interruptive military service.

4. Providing a disability benefit equal to the reduced accrued pension. (This benefit is used to offset the 50% of compensation benefit payable outside of the pension plan).

5. Removing the post-retirement death benefit and allowing the member to select an actuarial equivalent benefit option.

6. Changing the pre-retirement death benefit to return of the member’s accumulated contributions for members who are single or have less than ten years of service. For married member or one with an eligible child to a reduced accrued benefit or 150 percent of the member’s accumulated contributions at the survivor’s option.

In addition this bill provides that the funding of the plan shall be done on an aggregate actuarial cost method, as done for other plan 2's.

Effective Date: July 1,2001.

BACKGROUND DISCUSSION:

This changes the cola to the same used in other plan 2's. This is in most cases more favorable since it provides a 3% compound cola to the member and their beneficiary instead of the current 2% simple cola to the member. Only when the actual inflation is less than 2% on an accumulative basis would this provide for less of an increase. This is also likely to provide a better cola to the beneficiary than the current uniform cola increase.

The current employee rate fixed at 7% is similar to the fixed 6% rate for other Plan 1's. The splitting of the costs is similar to the other plan 2's. The 2% rate provides that current and new member's pay for a portion of their costs.

The other changes makes this plan more similar to the Law Enforcement and Firefighter's Retirement Plan 2 (LEOFF) for those who become members after July 1,2001.

MEMBERS IMPACTED:

We estimate that all of the 968 active, 15 deferred vested, 67 disabled, and 647 retired members of this system would be affected by this bill.

1. The average monthly benefit for a new retiree in this system was $3,124 in 1999. A 2% increase would be $62.48. A 3% increase would be $93.72. The total increase over ten years would be $624.80 for the simple 2% increase. The 3% compound increase would be $1,074.40 over ten years.

2. The average salary for the active member is $57,496. Contributions at 7% would be $4,024.72. Contributions at 2% would be $1,149.92. In the very long run, if the assumptions of the plan are realized, the cost of the new member is expected to be about 16.52%. The contributions at half this rate for the member (8.26%) would be $4,749.17

3. We do not have the data to estimate the average effect of eliminating voluntary overtime. This will have an effect on individuals who have a large amount of voluntary overtime in their last two years of employment.

For new members after January 1, 2003 we estimate:

1. The change from a 3 year to a 5 year average final salary would result in an average 6% decrease in benefits.

2. The elimination of cash outs from the salary included under the plan would result in approximately an 8% decrease in benefits.

3. The change in the military service provisions would result in a decrease in benefits of 9%. (Based on an average 2.5 years of military service for someone with 25 years of service: 2.5/27.5 = 9%).

4. There is currently no disability benefit payable from the pension plan. This provides a benefit equal to the accrued pension under the plan, reduced for early commencement. This benefit is an offset to the duty disability benefit received outside the plan.

5. The post-retirement death benefit is about 7% of the total cost of the plan. This will affect married members more than this, and will not affect members without beneficiaries.

6. The pre-retirement death benefit of 50% of the member's pay is replaced with a reduced accrued benefit or 150% of the member's accumulated contributions for the married member with ten years of service, and a return of 100% of the member's accumulated contributions for those with less than ten years of service. This is a much smaller death benefit, especially for those with a few years of service and/or those who have not attained the normal retirement age.

FISCAL IMPACT:

Actuarial Determinations:

Because the assets will continue to exceed the present value of projected benefits there is no immediate impact of these changes on the employer's contribution rates.

The benefit changes to new members will not have an affect until those members enter the plan and funding commences for them. The current cost for a new member is 19.68% - 7.00% or 12.68% of pay. Under the proposed plan the expected long term cost would be about half of 16.52% or 8.26% of pay for the employer and an equal amount to the employee. However until the plan is no longer fully funded this cost will be "funded" by the surplus in the plan and the employee's 2% contribution rate.

The change in the employee rate from 7% to 2% is expected to reduce the present value of employee contributions by $27.251 million for current members. This will accelerate the time when the plan will have to resume contributions, and/or the amount of those contributions.

The bill will impact the actuarial funding of the system by increasing the present value of benefits payable under the Washington State Patrol Retirement System and the required actuarial contribution rate as shown below:

Washington State Patrol Retirement System:

(Dollars in Millions)	**Current**	**Increase**	**Total**
Actuarial Present Value of Projected Benefits The Value of the Total Commitment to all Current Members	$545	$44	$589
Unfunded Actuarial Accrued Liability The Portion of the Plan 1 Liability that is Amortized until 2024	$(213)	$44	$(169)
Unfunded Liability (PBO) The Value of the Total Commitment to all Current Members Attributable to Past Service	$(246)	$26	$(220)
Required Contribution Rate	-8.28%	-7.15%	-15.43%

As stated above it is expected that the employer contribution rates would eventually rise to +8.26% as new members are added to the plan if our valuation assumptions are realized in the very long term. Without these changes the rate would be expected to rise to +12.70%.

The chart below illustrates the effect of these changes on the contribution rates of the current membership.

	Normal Cost	Employee Rate	Employer Rate	Amortization of Unfunded	Total Employer Rate
Current Rate	19.70%	7.00%	12.70%	-20.98%	-8.28%
Increase to Cola	22.64%	7.00%	15.64%	-18.42%	-2.78%
Change in Employee Rate	22.64%	2.00%	20.64%	-18.42%	2.22%
Change to Aggregate	-13.43%	2.00%	-15.43	NA	-15.43%

The table below shows the expected long-term change in the employer cost by looking at the change in the entry-age normal cost.

Current Employer Normal Cost	12.70%
Increase for 3% COLA	2.94%
Eliminate Prior Military Service	-1.65%
Eliminate Cash Outs & "voluntary" overtime	-1.45%
Change 3YR. AFC to 5YR. AFC	-1.18%
Disability	0.10%
Death Benefits	-1.95%
Change In Employee Contribution	-1.26%
Employer Rate for New Employees	8.26%

Fiscal Budget Determinations:

Because the value of assets exceeds the present value of fully projected benefits the required contribution rate remains at zero, even without the change to the aggregate method.

Gerald B. Allard, State Actuary

STATEMENT OF DATA AND ASSUMPTIONS USED IN PREPARING THIS FISCAL NOTE:

The costs presented in this fiscal bill are based on our understanding of the bill as well as generally accepted actuarial practices including the following:

1. Costs were developed using the same membership data, methods, assets and assumptions as those used in preparing the December 31,1999 actuarial valuation report of the Washington State Patrol Retirement System.

2. As with the costs developed in the actuarial valuation, the emerging costs of the System will vary from those presented in the valuation report or this fiscal note to the extent that actual experience differs from that projected by the actuarial assumptions.

3. Additional assumptions used to evaluate the cost impact of the bill which were not used or disclosed in the actuarial valuation report include the following:

   The long term cost of the pre-retirement death and disability benefits for new members was estimated using the entry-age costs for LEOFF 2.

4. The analysis of this bill does not consider any other proposed changes to the system. The combined effect of several changes to the system could exceed the sum of each proposed change considered individually.

5. This fiscal note is intended for use only during the 2001 Legislative Session.

6. The funding method used for Plan 1 utilizes the Plan 2 employer/state rate as the Normal Cost and amortizes the remaining liability (UAAL) by the year 2024. Benefit increases to Plan 2 will change the UAAL in Plan 1. The cost of benefit increases to Plan 1 increases the UAAL.

   Costs were shown amortizing the surplus by the year 2024. Because the plan is fully funded the rate is zero and no amortization is occurring.

7. Plan 2 utilizes the Aggregate Funding Method. The cost of Plan 2 is spread over the average working lifetime of the current active Plan 2 members.

GLOSSARY OF ACTUARIAL TERMS:

Actuarial Present Value: The value of an amount or series of amounts payable or receivable at various times, determined as of a given date by the application of a particular set of Actuarial Assumptions.

Projected Benefits: Pension benefit amounts which are expected to be paid in the taking into account such items as the effect of advancement in age and past and anticipated future compensation and service credits.

Unfunded Actuarial Accrued Liability(UAAL): The cost of Plan 1 is divided into two pieces. The Normal Cost portion is paid over the working lifetime of the Plan 1 active members. The remaining cost is called the UAAL. The UAAL is paid for by employers as a percent of the salaries of all plan 1, 2 and 3 members until the year 2024.

Pension Benefit Obligation (PBO): The portion of the Actuarial Present Value of future benefits attributable to service credit that has been earned to date(past service).

Unfunded Liability (Unfunded PBO): The excess, if any, of the Pension Benefit Obligation over the Valuation Assets. This is the portion of all benefits earned to date that are not covered by plan assets.

Uniform COLA at Age 66
Bill Summary

Currently a retired member of PERS plan 1 or TRS plan 1 is first eligible to receive the annual increase to their retirement allowance in the calendar year that they have both been retired for one year and are age 66 by July 1st.

The draft bill language changes the requirement that the retired member be age 66 by July 1st to a requirement that they be age 66 by December 31st in the calendar year in which the annual increase is given.

FISCAL NOTE

REQUEST NO.

RESPONDING AGENCY:	CODE:	DATE:	BILL NUMBER:
Office of the State Actuary	**035**	**10/24/00**	**Z-0224.5/01**

SUMMARY:

This bill impacts the Public Employees' Retirement System (PERS) Plan 1 and Teachers' Retirement System (TRS) Plan 1 by allowing those who have been retired for one year, and will be at least age 66 by December 31st, to receive the annual increase paid on July 1st of that year.

Effective Date: July 1, 2001.

BACKGROUND DISCUSSION:

The current provision requires the member to have been retired one year and to be at least age 66 on July 1st to eligible for the annual increase paid that year. This means that some members will get their first COLA as early as age 66, while others will not get theirs until age 67 (or one to two years after retirement if later). This bill would change this so that some members would get their COLA as early as age 65½, while others will not get theirs until age 66½ (or one to two years after retirement if later).

MEMBERS IMPACTED:

We estimate that 50% of the members who are under age 65 would be affected by this bill.

TRS Plan 1	Under Age 65	Total
Receiving a Benefit	8,196	28,920
Actives	18,525	18,737
Vested Terminated	2,071*	2,071

PERS Plan 1	Under Age 65	Total
Receiving a Benefit	10,446	52,515
Actives	27,390	28,168
Vested Terminated	3,295*	3,295

******All are assumed to be under age 65.*

We estimate that for a typical member impacted by this bill, the annual increase would be paid one year earlier. The annual increase for July 1, 2001 in the monthly benefit is $1.11 times years of service. The annual increase is increased by 3% each year and by future "gain-sharing" amounts. The typical recipient of the Uniform COLA has 19 years of service in PERS and 25 years of service in TRS.

FISCAL IMPACT:

Actuarial Determinations:

The bill will impact the actuarial funding of the system by increasing the present value of benefits payable under the System and the required actuarial contribution rate as shown below:

Teachers' Retirement System and Public Employees' Retirement System (Plan 1):

(Dollars in Millions)	**System:**	**Current**	**Increase**	**Total**
Actuarial Present Value of Projected Benefits The Value of the Total Commitment to all Current Members	PERS 1 TRS 1	$12,494 10,382	$ 36 32	$ 12,530 10,414
Unfunded Actuarial Accrued Liability The Portion of the Plan 1 Liability that is Amortized until 2016	PERS 1 TRS 1	$ 1,589 1,263	$ 36 32	$ 1,625 1,295
Unfunded Liability (PBO) The Value of the Total Commitment to all Current Members Attributable to Past Service	PERS 1 TRS 1	$ 809 663	$ 32 28	$ 841 691
Required Contribution Rate-Employer/State	PERS TRS	3.21% 5.38%	.04% .09%	3.25% 5.47%

Fiscal Budget Determinations:

As a result of the higher required contribution rate, the increase in funding expenditures is projected to be:

	PERS/SERS	**TRS**
Increase in Contribution Rates:		
Effective 9/1/2001		
Employee (Plan 2)	0.00%	0.00%
Employer	0.04%	0.08%

	PERS/SERS	TRS
Costs (in Millions):		
2001-2003		
State:		
General Fund	$ 1.4	$ 4.1
Non-General Fund	1.6	0.0
Total State	**$ 3.0**	**$ 4.1**
Local Government	$ 2.7	$ 0.9
2001-2005		
State:		
General Fund	$ 3.0	$ 8.7
Non-General Fund	3.5	0.0
Total State	**$ 6.5**	**$ 8.7**
Local Government	$ 5.9	$ 2.0
2001-2017		
State:		
General Fund	$ 16.5	$ 46.3
Non-General Fund	19.1	0.0
Total State	**$ 35.6**	**$ 46.3**
Local Government	$ 32.7	$ 10.5

Gerald B. Allard, State Actuary

Washington State Patrol

Background:

As a result of legislation passed in the 2000 session, the WSP employee contribution rates were lowered from 7% to 3% for the July 1, 2000 through June 30, 2001 period. During this period, the JCPP was directed to"...study the Washington State Patrol Retirement System..."

The Washington State Patrol Retirement System (WSPRS) was created on June 12, 1947. The WSPRS provides a guaranteed benefit to eligible Patrol members and their survivors based on a formula which multiplies the member's years of service, by their average final salary (AFS) and 2%, with a maximum benefit not to exceed 75 percent of their AFS.

The WSPRS is currently the only state administered plan that still contains many of the plan provisions that were altered or eliminated under the Plan 2/3 systems. These include:

- Service-based retirement eligibility
- Credit for prior military service with no cost to the member
- Two-year average final salary used in calculating retirement benefits
- Disability and death benefits not based on service
- Survivor benefits provided at no cost to the member
- Inclusion of annual and holiday leave cash-out in calculation of AFS

Committee Activity:

Presentation: WSP System Report
May 25, 2000, Full Committee Meeting
Roundtable Discussion: WSP System
June 21, 2000, Full Committee Meeting
Presentation: Proposal, Public Testimony
November 15, 2000, Full Committee Meeting
Presentation - Proposal Approved:
December 13, 2000, Full Committee Meeting

Recommendation to Legislature:

The Washington State Patrol Retirement System employee contribution rate for new and existing members is to be 2% or equal to the employer rate, whichever is greater. The duty disability retirement for new members is to include the member's accrued pension. The non-duty disability retirement for new members is to be the member's accrued pension actuarially reduced. The calculation of average final salary for new members is to be a 60 month average. The definition of salary for existing members is to prospectively exclude voluntary overtime. The definition of salary for new members is to exclude voluntary overtime and annual and holiday cash-outs. The military service credit for new members is to be 5 years of interruptable service with member payment of contributions. Retirement payment options for new members are to be expanded. Survivor benefits for new members are to be the member's accumulated contributions or an accrued pension actuarially reduced. The minimum retirement allowance is to increase 3% per year. The WSP employer contribution rate is to be calculated by the aggregate actuarial cost method.

Staff Contact:

Robert Wm. Baker - 586-9237 – baker_bo@leg.wa.gov

Washington State Patrol Retirement System Report

Joint Committee on Pension Policy
Revised December 19, 2000

Prepared by:

Robert Wm. Baker
Senior Research Analyst

I. Introduction:

In 1999, employer and employee contribution rates in the Washington State Patrol Retirement System (WSPRS) emerged as an issue. Because of the sound funding status of the WSPRS system, employer contribution rates fell to 0% in 1999.

Within the Transportation Budget were directives for the Joint Committee on Pension Policy (JCPP) to study the method for setting employer and employee contribution rates. The JCPP studied the issue and recommended that employee contribution rates be lowered from 7% to 3% for the July 1, 2000 through June 30, 2001 period. And in approving the Washington State Patrol Contribution Rates Report, the JCPP was also directed to ”... study the Washington State Patrol Retirement System (WSP) during the 2000 Interim...”

This document represents a brief summary of the demographics of plan members, major provisions of the WSPRS as contained in RCW Chapter 43.43 and how they compare with the only other open law enforcement related retirement plan --LEOFF 2, and features of the system that make it unique among the state administered retirement plans.

II. Background:

The Washington State Patrol Retirement System (WSPRS) was created on June 12, 1947. This system provides a guaranteed benefit to eligible Patrol members and their survivors based on a formula which multiplies the member's years of service, by their average final salary (AFS) and 2%, with a maximum benefit not to exceed 75% of their AFS.

At this time there are several retirement plans administered by the State for public employees who serve in public safety activities. In addition to the WSPRS, there are the Law Enforcement Officers and Fire Fighters (LEOFF) Plans 1 and 2.

The WSPRS is currently the only state-administered plan that still contains many of the plan provisions that were altered or eliminated under the Plan 2/3 systems. These include:

- Service-based retirement eligibility
- Credit for prior military service with no cost to the member
- Two-year average final salary used in calculating retirement benefits
- Disability and death benefits not based on service
- Survivor benefits provided at no cost to the member
- Inclusion of annual and holiday leave cash-out in calculation of AFS.

A. Demographics:

Comparative summary statistics on WSPRS active membership, annuitants, and survivors are displayed below (data as of December 31, 1999). At the end of 1999 there were 968 active, 537 service retirees, and 110 survivor members of the WSPRS.

Membership Demographics 1999

	Active	Retirees	Survivors
Number	968	537	110
Average Age	38.4	61.2	71.8
Average YOS	12.5	28.8	11.7
Average Annual Salary/Benefit	$ 57,496	$ 32,325	$ 11,931
Salary/Benefit Increase From Prior Year	4.8%	3.9%	6.2%

III. Review of Differences in Plan Features:

Statutory provisions vary between each of the state-administered retirement plans. This results in a wide range of actuarial differences amongst the several plans, such as employer and employee contribution rates, unfunded liability and funding ratios, and member demographics.

In addition to the actuarial distinctions, there are qualitative differences that result from the dissimilar features of the various plans. The features within the WSPRS that are not available to members of the current plan 2/3 systems include:

A. Service-based retirement eligibility:

At this point a WSPRS member is eligible for full retirement after serving 25 years regardless of age. Retirement eligibility provisions in all other currently open plans are primarily based on age.

As a result of these provisions, the WSPRS has the youngest normal retirement age of all the open Washington state pension plans. A comparison of retirement ages and years of service for service retirees by plan is in the following table:

Average Retirement Age and Years
Experience Period Ending 1999

Plan	Average Age	Years of Service
WSPRS	51	28.4*
PERS 1	60	25.1*
PERS 2	66	12.2
TRS 1	58	28.7
TRS 2/3	65	13.1
LEOFF 1	54	27.7
LEOFF 2	59	12.3

**Includes Military Service.*

B. Credit for prior military service at no cost to the member:

WSPRS members with 25 years of service credit can receive up to five years of credit for prior military service. PERS 1 is the only other plan to offer this benefit. In all other currently open plans a member may receive credit for up to five years of interruptive military service if they pay the necessary employee contributions. This allowance will increase the total service credit and thus the benefit calculation.

For those WSPRS members who retired in 1999, some 46% had prior military service added to their service credit. As a comparison, of the PERS 1 members who retired in the most recently available year, about 20% had military service added to their service credit.

Military Service		
	PERS 1	**WSPRS**
Percent with military service	19.8%	45.7%
Average months of military service	7.3	14.7
Average for those with military	36.6	32.3
Benefit per year per member	$ 515	$ 1,603
Benefit per year per member with military	$ 3,200	$ 3,324

C. Two-year average final compensation used in calculation of retirement benefit:

WSPRS member's average monthly salary of the highest two consecutive years is used to calculate their average final salary (AFS). All other currently open plans use the monthly average compensation of the highest 60 consecutive months.

D. Inclusion of annual and holiday leave cash-out and other pay in calculation of AFS.

WSPRS member's compensation for determination of their average final salary may include the lump-sum cash-outs for unused annual and holiday leave. Compensation in all other open plans excludes lump-sum payments for sick leave, vacation, annual leave, or any form of severance pay.

Also, included in AFS for WSPRS members is any overtime pay. In LEOFF 1 there is specific language excluding overtime pay from the AFC calculation. This can result in pay patterns in WSPRS that are unlike those in other plans.

Annual Salary Increases for 1999 Retirees by Select Plan: 1994-1998

PLAN	1994	1995	1996	1997	1998	Last 2 yrs
LEOFF 1	5.7%	4.5%	2.9%	4.8%	3.2%	8.2%
PERS 1	5.3%	1.0%	3.1%	4.2%	4.1%	8.5%
TRS 1	1.0%	1.5%	4.4%	1.1%	5.2%	6.4%
WSPRS	2.6%	4.5%	6.7%	7.8%	6.5%	14.9%

The use of overtime as a means of augmenting the WSPRS members salaries prior to retirement was examined by the Joint Legislative Audit and Review Committee (JLARC) with assistance by the Office of the State Actuary. In their report #99-4, the committee found,...that “the average WSPRS retiree had an estimated salary of $46,977 and an average final compensation of $57,633, which was 23 percent above the final two-year regular salary. An estimated 60% of that 23% was attributable to overtime earnings in the last two years of employment.”

E. Duty and non-duty disability retirement benefits:

"The chief of the Washington state patrol shall relieve from active duty Washington state patrol officers who, while in the performance of their official duties, or while on standby or available for duty, have been or hereafter may be injured or incapacitated to such an extent as to be mentally of physically incapable of active service:..." RCW 43.43.040

Though not a part of the formal WSPRS--benefits are paid from the operational funds of WSP-- members may receive a duty and non-duty related disability retirement benefit equal to 50% of their compensation regardless of service time. No currently open plan offers such a benefit.

Consider, also, that there are varying degrees of disability. While a WSPRS member may become disabled to the extent that they are unable to perform their duties as a State Patrol officer, that does not mean they are unable to perform some other gainful activity. As illustration, only four of the disabled WSPRS members receive an actual L&I pension. That is significant because a duty disability in the WSP system is reduced by any benefit received from industrial insurance.

As of December 31, 1999, there were 67 disability retirees. Of these approximately 50 were duty-related and 17 were non-duty related. The average annual disability allowance is approximately $23,000. A simple means of comparing the various plans is by examining the share of disability retirees. The percent is the number of disabled retirees divided into the total active and retired members within each system. The WSPRS and Plan 1 systems have disability benefits that are not actuarially reduced. The disability benefits under the Plan 2 systems are actuarially reduced. At this point, no Plan 2 employees are receiving disability retirement benefits.

Retirees in Select Washington Plans By Disability Status December 31, 1999	WSPRS	PERS 1	PERS 2	TRS 1	TRS 2	LEOFF 1	LEOFF 2
Total Service & Disability Retirees	604	46,321	6,460	26,841	380	6,552	97
Service Retirees	537	44,449	5,672	26,013	347	2,338	87
Disability Retirees	67	1,872	788	828	33	4,214	10
Duty	50	128	0	-na-	-na-	3,574	0
Non-duty	17	1,744	788	-na-	-na-	640	10
Disability % of Total Retirees	11.1%	4.0%	12.2%	3.1%	8.7%	64.3%	10.3%
Duty % of Disability Retirees	74.6%	6.8%	0.0%	-na-	-na-	84.8%	0.0%
Non-duty % of Disability Retirees	25.4%	93.2%	100.0%	-na-	-na-	15.2%	100.0%

In statute, TRS disabilities are categorized as “Temporary” or Permanent” rather than “Duty” or Non-Duty”. DRS codes all Plan 1 disabilities as “Duty” and all Plan 2 disabilities as “Non-Duty”.

F. Survivor benefit provided at no cost to the member:

The surviving spouse of a WSPRS member is eligible to receive 50% of AFS throughout the spouses life, and there are supplemental provisions for surviving children. Survivor benefits are available under all currently open plans, but are based on member contributions and retirement eligibility criteria. A survivor of a WSPRS member would receive the benefit regardless of the member's time in service. In addition, unlike LEOFF 1 members, WSPRS members can designate a spouse from a post-retirement marriage as their survivor.

G. Retirement Allowance Payment Options:

Until recently, there were limited retirement allowance payment options for WSPRS members. While more options are now currently available, the sections covering these provisions are still not entirely comparable to those found governing the Plan 2/3 systems. As a result, several provisions are not found in the WSPRS including: the option allowing the designation of a non-spouse as a survivor, the provisions governing the designation of a survivor beneficiary when there is a property division obligation, and the requirement for the written consent of a spouse to the payment option selected

H. Post Retirement Adjustment (COLA)

Each July 1st following retirement WSPRS members receive an increase of 2% of the initial service retirement allowance. Each April 1st, in LEOFF 1, retired members receive a COLA based on the Seattle Consumer Price Index (CPI). Each July 1, in PERS 1 and TRS 1, retired members receive a Uniform

COLA based on their months of service. Each July 1, in the Plan 2/3 systems, retired members receive a COLA based on the Seattle CPI to a maximum of 3%.

WSPRS is the only plan in which the post-retirement adjustment differs between the retiree and a beneficiary: A WSPRS survivor receives a Uniform COLA instead of the 2% increase in initial service retirement allowance.

I. No Contribution to Social Security:

Some employer groups in municipalities and counties may opt out of paying into the Social Security system. Many have established alternative plans; so LEOFF members may or may not pay into Social Security. But for all those considered state employees, only WSPRS members do not pay into the Social Security system.

J. Minimum Retirement Allowance:

Other Plan 1 systems guarantee a minimum benefit amount. It is typically a fixed dollar amount multiplied by month, by year of service. In July of 1997 the minimum retirement benefit for the WSPRS was set at $20 per month per year of service. Each year the minimum is adjusted by a fixed amount called the "annual increase amount." As of July 1, 1999 the annual increase amount was 77 cents.

IV. Other Provisional Differences:

Other provisional differences that have been a part of the WSPRS but not included in any other state-administered retirement system include:

A. Mandatory Retirement:

Except for the Washington State Patrol Chief, commissioned officers are subject to mandatory retirement at age 60. No other open plan has a mandatory retirement clause.

B. Unlimited Post Retirement Employment:

For those commissioned in the State Patrol prior to March 1976, there are no provisions restricting post retirement employment in the WSPRS. This, along with the dual membership provisions, allows a WSPRS retiree to be re-employed with no loss of benefits, even in a WSP position. In PERS, a retiree must wait a minimum of one month, and then is allowed to work up to five months per calendar year. In LEOFF 2, benefits will be suspended if a member returns to work in an eligible position in LEOFF, TRS, or PERS.

Again as part of their audit, the JLARC examined the post retirement employment issue. They examined the experience of 90 recent WSP retirees and found:

- 40% returned to employment with the State of Washington in a PERS 1 position
- 27% returned to employment with the WSP
- Most were rehired within six weeks of retirement

By being able to engage in this kind of post-retirement employment, the JLARC found a disincentive to remaining employed as WSP commissioned officers. This disincentive is significant because by becoming re-employed in a PERS 1 eligible position, and working an additional 13 years, a WSPRS member can realize an additional $11,425 in annual retirement benefits.

C. Overall Retirement Benefits:

The WSPRS has the highest benefit for actual months of service of any of the state administered retirement plans. The reasons for this benefit consist of not only the good salaries paid to commissioned officers but the inclusion of overtime, lump sum payments for unused annual and holiday pay, credit for prior military service, and use of a two-year average in calculating AFC.

Retirement Benefit per Actual Month of Service

Plan	FAS	Benefit/ Month	Benefit/ Month/YOS
LEOFF 1	$63,994	$ 3,069	$ 107.15
PERS 1	$42,535	$ 1,816	$ 71.21
TRS 1	$53,252	$ 2,484	$ 85.84
WSPRS	$65,254	$ 3,098	$ 113.64

V. Summary:

The features of the Washington State Patrol Retirement System make it distinct from other State administered retirement plans. Its longevity alone (53 years) gives it a unique status; no other open plan has been in place longer than 23 years. As a result, the records of WSPRS members and annuitants are more historically complete than the closed Plan 1 systems, or the currently open plans. Beyond its duration, the other features that make the WSPRS unique are those that were specifically excluded from the more recent plans; features that would not likely be possible without the high level of state funding in support of the system.

VI. Proposal:

A. Contribution Rate:

During the last legislative session, the employee contribution rate was temporarily reduced to 3.00% while the JCPP studied the plan features. The rate will return to the previous statutory rate of 7.00% on July 1, 2001 if there is no additional legislative action.

Existing Members: 2.00%, or equal to the employer rate, whichever is greater.

New Members: 2.00%, or equal to the employer rate, whichever is greater.

B. Post Retirement Adjustment (COLA):

The post retirement adjustment for current members is a simple 2.00% adjustment that occurs on July 1 of each year. Because it is a simple adjustment, the results do not compound.

Existing Members: (Including current retirees and survivors): Annual compounded adjustment each July based on Seattle-Tacoma-Bremerton CPI-W to a maximum of 3%.

New Members: (Including survivors): Annual compounded adjustment each July based on the Seattle-Tacoma-Bremerton CPI-W to a maximum of 3%.

C. Military Service Credit:

Existing members, after 25 years of service, are allowed to include up to 5 years of prior military service in their benefit calculation.

Existing Members: No Change

New Members: No prior military service is included. May include 5 years of interruptive military service in their benefit calculation.

D. Compensation used in Calculating Average Final Salary:

Current members include, in addition to their regular salary, all over-time pay and annual and holiday pay cash-outs in calculating their average final salary.

Existing Members: Salary earned, including administrative overtime and cash-outs, but excluding "voluntary" overtime prospectively.

New Members: Salary earned, including administrative overtime, excluding "voluntary" overtime, and excluding cash-outs.

E. Computation of Average Final Salary:

Current members use the average monthly salary of the highest two consecutive years in the computation of their average final salary.

Existing Members: No change

New Members: The monthly average compensation of the highest 60 consecutive months.

F. Duty Disability:

Current members may receive a duty disability allowance equivalent to 50% of their compensation at the existing wage, less any compensation received from Labor and Industries. This allowance is paid from the operating funds of the Washington State Patrol, not from the retirement system.

Existing Members: No change.

New Members: The greater of 50% of compensation at the existing wage, or Labor and Industries payments and accrued pension.

G. Non-Duty Disability:

Current members may receive a non-duty disability allowance of 50% of their compensation at the existing wage. If under age 50, the allowance may be reduced if the combination of allowance and compensation received from gainful employment exceeds the basic salary of the rank held at the time of disablement. This allowance is paid from WSP operating funds, not from the retirement system.

Existing Members: No change.

New Members: An accrued pension actuarially reduced from age 55 or from the member's 25th year of service, whichever is less.

H. Survivor Benefits:

Survivor benefits for active members consists of 50% of the member's AFS throughout the spouses life, with additional provisions for children. Survivor benefits for retired members consists of the lesser of 50% of the AFS or the allowance paid to the member, again with additional provisions for children.

Existing Members: No change.

New Members: An active member benefit shall be an accrued pension actuarially reduced from age 55 or from when the member could have reached their 25th year of service, whichever is less. A retired member survivor benefit will be a joint and survivor benefit option chosen at the time of retirement.

I. Retirement Allowance Payment Options:

Current members now are able to chose among the standard joint and survivor benefits offered by the Department of Retirement Systems.

Existing Members: No change.

New Members: Enhance existing provisions to include the option of allowing the designation of a non-spouse as a survivor. Limit the survivor beneficiary designation when there is a property division obligation. Require written consent of a spouse to the payment option selected.

WSPRS Benefits Proposal

Member Years of Service	Contribution Rate	COLA	Military Service Credit	Compensation	Computation of AFS	Disability	
						Duty	Non-duty
Existing Members	Change To 2.00%min. or equal to employer rate	Change To 3% maximum	No Change 5 yrs prior	Change To Salary earned (includes OT and cash-outs, excl. "voluntary" OT prospectively[1])	No Change 2 year avg	No Change 50% of comp. at existing wage, less L&I	No Change 50% of comp, less gainful earnings that exceed salary at time of disability.
New Hires	Change To 2.00% min. or equal to employer rate	Change To 3% maximum	Change To No prior. 5 yrs interruptive[2]	Change To Salary (includes admin. OT, excl. "voluntary" OT, and cash-outs[3])	Change To 5 year avg	Change To The greater of 50% of comp. at existing wage, or L&I and accrued pension	Change To Accrued pension actuarially reduced

Fiscal Impact: The change for existing members does not take the plan out of full funding.
The employer cost of the proposed benefits for future hires will be approximately 75% of the cost of the current set of benefits for future hires.

Note: No change in requirements for service retirement; still 25 years of credited service, or age 55.

[1] "Voluntary" overtime allowed up to the date of the act and not allowed thereafter.

[2] All plan members are allowed to purchase interruptive military service as per federal law.

[3] Members can still receive cash-outs upon retirement, but they won't be included in the computation of AFS.

Appendix A

Washington State Patrol Retirement System Plan Provisions

Membership: Membership in the WSPRS is mandatory for commissioned members of the Washington State Patrol (WSP). This system currently remains open to new membership.

Dual membership: Dual membership exists if previous membership retained or established in LEOFF 2, PERS, TRS, SERS, Statewide City Employees' Retirement System (SCERS), or the retirement systems of Seattle Spokane, or Tacoma.

Vesting: Established upon completion of five years of credited service.

Terminated, vested benefit: ... member may receive a normal retirement allowance upon attainment of age 60, or an actuarially reduced allowance at age 55.

Credited service: All calendar months of full-time employment during which salary is paid for 70 or more hours. PERS Plan 1 or Plan 2 credited service earned as a Washington State Patrol Cadet may be transferred upon transfer of necessary contributions and interest.

Service Credit for Leave of Absence: No provision.

Military Service Credit: A member with 25 years of credited service may receive up to five years credit for prior military service. A member whose service is interrupted by active duty military service and who resumes employment as a member of WSPRS within one year of discharge from the armed forces will receive up to five yeas service credit for military service.

Withdrawal of Employee Contributions: Upon termination of employment for reasons other than retirement or disability a member may sever relationship with the system by withdrawing their employee contributions, plus accrued interest thereon.

Restoration of Withdrawn Contributions: Withdrawn contributions, plus interest, may be restored within ten years of the date of termination and five years of the date of resuming service. If restoration is based on dual membership, restoration must be made within two years of establishing dual membership or prior to retirement, whichever occurs first.

Compensation: The salary earned as a commissioned officer.

Computation of Average Final Compensation: The average monthly salary of the highest two consecutive years; or, if credited service is less than two years, the average monthly salary of the total service. (Defined as [AFS]).

Requirements for Service Retirement: Completion of 25 years of credited service or Attainment of age 55. Except for the Chief, WSP, retirement is statutorily mandatory upon attainment of age 60.

Service Retirement Allowance: 2% of AFS for each year of credited service not to exceed 75% of AFS.

Minimum Benefit: $20 per month, per year of service.

Post-Retirement Adjustment: Each July 1st following retirement and increase of 2% of the initial service retirement allowance is provided to the member. (The surviving beneficiary does not receive this adjustment.)

Retirement for Disability: Both the Duty and Non-duty disability benefits are paid from the operational funds of WSP.

Duty: 50% of current compensation, less any benefit received from industrial insurance.

Non-duty: An earned retirement benefit. If less than age 50, then may be reduced so that the sum of the allowance and the compensation received form gainful employment does not exceed the basic salary of the rank held at the time of disablement.

Survivor Benefits - Active Members: The surviving spouse receives 50% of AFS throughout the spouses life, with subsequent marriage qualifications.

If there are surviving children, an additional 5% of AFS for each child is provided except the total benefit may not exceed 60% of AFS.

In the event of no surviving spouse, the first surviving child receives 30% of AFS and each additional child receives 10% of AFS except that the total benefit may not exceed 60%. Allowance is prorated among the children. The children become ineligible at age 18. If the member dies in the line of duty, the benefit to the child(ren) continues to age 21 if they are attending school.

Survivor Benefits - Retired Members: The surviving spouse receives the lesser of 50% of AFS or the allowance paid to the member, with subsequent marriage qualifications.

If there are children, an additional 5% of AFS is provided per child except the total may not exceed 60%.

In the event of no surviving spouse, the first surviving child receives 30% of AFS and each additional child receives 10% of AFS except that the total benefit may not exceed 60%. Allowance is prorated among the children. The children become ineligible at age 18.

Post-Retirement Employment: No provision. Retirees may be employed as members of other state retirement systems without suspension of benefits.

Member Contributions and Funding: 7% of compensation.

Employer Contributions and Funding: See State Contributions and Funding

State Contributions and Funding: The "normal contribution" (i.e., normal cost) and an "unfunded liability contribution" as calculated by the office of the State Actuary.

Appendix B

WSPRS and LEOFF 2 Provisional Differences

Dual Membership

WSPRS	LEOFF 2
Dual membership exists if previous membership retained or established in LEOFF 2, PERS, TRS, SERS, Statewide City Employees' Retirement system (SCERS), or the retirement systems of Seattle, Spokane, or Tacoma.	No provision.

Military Service Credit

WSPRS	LEOFF 2
A member with 25 years of credited service may receive up to five years credit for prior military service. A member whose service is interrupted by active duty military service and who resumes employment as a member of WSPRS within one year of discharge from the armed forces will receive up to five yeas service credit for military service.	A member may receive credit for up to five years of interruptive service in the military by paying the necessary employee contributions.

Computation of Average Final Compensation

WSPRS	LEOFF 2
The average monthly salary of the highest two consecutive years; or, if credited service is less than two years, the average monthly salary of the total service. (Defined as [AFS]).	The monthly average compensation (i.e., basic salary) of the highest 60 consecutive service credit months. (Defined as *final average salary* or *FAS* rather than *AFC*.)

Requirements for Service Retirement	
WSPRS	**LEOFF 2**
Completion of 25 years of credited service or Attainment of age 55.	Five service credit years of service and attainment of age 53; or Attainment of age 50 and completion of 20 service credit years, with the benefit reduced 3% per year between retirement age and from age 53.

Service Retirement Allowance	
WSPRS	**LEOFF 2**
2% of AFS for each year of credited service not to exceed 75% of AFS.	2% of FAS for each year of credited service without limit.

Retirement for Disability	
WSPRS	**LEOFF 2**
Both the Duty and Non-duty disability benefits are paid from the operational funds of WSP. Duty. 50% of current compensation, less any benefit received from industrial insurance. Non-duty. An earned retirement benefit. If less than age 50, then may be reduced so that the sum of the allowance and the compensation received form gainful employment does not exceed the basic salary of the rank held at the time of disablement.	A member who becomes totally incapacitated for continued employment shall receive an allowance based upon service credit years and actuarially reduced from age 55.

Survivor Benefits - Active Members

WSPRS	LEOFF 2
The surviving spouse receives 50% of AFS throughout the spouses life, with subsequent marriage qualifications. If there are surviving children, an additional 5% of AFS for each child is provided except the total benefit may not exceed 60% of AFS. In the event of no surviving spouse, the first surviving child receives 30% of AFS and each additional child receives 10% of AFS except that the total benefit may not exceed 60%. Allowance is prorated among the children. The children become ineligible at age 18. If the member dies in the line of duty, the benefit to the child(ren) continues to age 21 if they are attending school.	If the decedent was not eligible to retire, and had less than ten years of service, the member contribution, plus interest, are refunded to: a designated beneficiary; trust; organization; or the member's estate. If the decedent had at least ten years of service of was eligible to retire, the surviving spouse, or child(ren) if no spouse, may elect either a refund of 150% of contributions, plus accrued interest, or a monthly allowance.

Survivor Benefits - Retired Members

WSPRS	LEOFF 2
The surviving spouse receives the lesser of 50% of AFS or the allowance paid to the member, with subsequent marriage qualifications. If there are children, an additional 5% of AFS is provided per child except the total may not exceed 60%. In the event of no surviving spouse, the first surviving child receives 30% of AFS and each additional child receives 10% of AFS except that the total benefit may not exceed 60%. Allowance is prorated among the children. The children become ineligible at age 18.	At the time of retirement for service of disability, the member, with the written consent of the member's spouse, may choose among survivor options adopted bu DRS. If spousal consent is not provided, DRS will provide a benefit as if a joint and 50% option was taken.

Post-Retirement Employment

WSPRS	LEOFF 2
For those commissioned prior to March 1976, upon retirement may be employed as members of other state retirement systems without suspension of benefits.	Retirement benefits will be suspended if employed in an eligible position within LEOFF, TRS, or PERS. Retirees are permitted to work in any ineligible position within these systems.

Other WSPRS and LEOFF 2 Provisional Differences

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Terminated, Vested Benefit (terminates but maintains membership by not withdrawing contributions)

WSPRS	LEOFF 2
... member may receive a normal retirement allowance upon attainment of age 60, or an actuarially reduced allowance at age 55.	... member may receive a service retirement allowance upon attaining age 53.

Credited Service

WSPRS	LEOFF 2
All calendar months of full-time employment during which salary is paid for 70 or more hours.	A service credit month is earned for all calendar months of employment for which compensation is received for 90 or more hours.

Service Credit for Leave of Absence

WSPRS	LEOFF 2
No provision.	A member who is no paid leave of absence will receive service credit for such leave. A member taking unpaid authorized leave of absence, upon return to service, may make the member, employer, and state contributions with interest, and thereby receive up to two service credit years in a working career. A member who qualifies for workers compensation payments and disability leave supplement may also qualify for service credit up to six months leave of absence.

Withdrawal of Employee Contributions

WSPRS	LEOFF 2
Upon termination of employment for reasons other than retirement or disability a member may sever relationship with the system by withdrawing their employee contributions, plus accrued interest thereon.	If a member has less than ten years of service, the member may sever their relationship with the system by withdrawing their employee contributions, plus accrued interest. If a member has ten years of more of service, the member may request a refund of 150% of contributions, plus accrued interest thereon, and thereby sever relationship with the system.

Restoration of Withdrawn Contributions

WSPRS	LEOFF 2
Withdrawn contributions, plus interest, may be restored within ten years of the date of termination and five years of the date of resuming service. If restoration is based on dual membership, restoration must be made within two years of establishing dual membership or prior to retirement, whichever occurs first.	Withdrawn funds, plus interest, are to be restored within five years of the date of re-entering membership or prior to retirement, whichever occurs first. If contributions are not restored within five years, members must pay full actuarial value of restored service.

Compensation

WSPRS	LEOFF 2
The salary earned as a commissioned officer.	Salaries and wages earned during a payroll period for personal services, including overtime payments and deferred compensation, but excluding lump sum payments for sick leave, vacation, annual leave, or any form of severance pay.

Minimum Benefit

WSPRS	LEOFF 2
$20 per month, per year of service.	No provision.

Post-Retirement Adjustment

WSPRS	LEOFF 2
Each July 1st following retirement and increase of 2% of the initial service retirement allowance is provided to the member. (The surviving beneficiary does not receive this adjustment.)	Each July 1st, after one year of retirement, the allowance is adjusted to a maximum of 3%, based on the CPI-Seattle.

Member Contributions and Funding

WSPRS	LEOFF 2
7.0% of compensation.	Half the cost of LEOFF 2

Employer Contributions and Funding

WSPRS	LEOFF 2
See State Contributions and Funding	Employers pay 30% of the cost of LEOFF 2 (with provisions for excess compensation).

State Contributions and Funding

WSPRS	LEOFF 2
The "normal contribution" (i.e., normal cost) and an "unfunded liability contribution" as calculated by the office of the State Actuary.	20% of the cost of LEOFF 2.

Appendix C

Funding Ratios and Contribution Rates

There are two standard measures of funding status: the unfunded liability (or surplus) and the funding ratio. These measures are not used in the calculation of contribution rates, but are valuable in evaluating the funding status of a system. Plans that are properly funded from their inception should, and almost always will, have no unfunded liabilities. Similarly, they will have funding ratios greater than 100%. When a plan does not meet this goal, it is usually the result of a retroactive benefit increase. Ongoing economic and demographic experience have also had dramatic impacts on the funding results.

Development of Funding Ratio
(Based on YOS earned to date 1999)

Present Value of Credited Projected Benefits	(a)	$417 Million
Market Value of Assets	(b)	$662 Million
Unfunded Present Value of Benefits (Surplus)	(a - b)	($246) Million
Funding Ratio	(b ÷ a)	159%

As the table above indicates, the market value of assets exceeds the current value of retirement benefits expected to be paid out in the future (based on projected salaries and the amount of service members have earned through 1998) by $184 million.

Funding Ratios Comparisons:

As mentioned above, the funding ratio is a good indicator of the financial soundness of a retirement plan. Tracking the funding ratio over time allows an evaluation of the movement toward or away from a system's financial health.

The funding ratios of the various plans differ significantly. Only the Plan 1 systems have unfunded liabilities and, therefore, funding ratios under 100%. This was a result of under-funding and major retroactive benefit increases granted during the 1970s and 1980s. Plus an unfunded liability already existed when the state assumed responsibility for local government's police and fire fighter retirement plans.

Comparisons of Funding Ratios by Plan 1994-1998						
Plan	**1994**	**1995**	**1996**	**1997**	**1998**	**1999**
PERS 1	68%	68%	73%	83%	86%	93%
PERS 2	140%	149%	157%	187%	191%	189%
TRS 1	65%	65%	70%	82%	86%	93%
TRS 2/3	130%	136%	144%	181%	185%	188%
LEOFF 1	68%	80%	89%	108%	117%	125%
LEOFF 2	124%	126%	130%	155%	160%	154%
WSPRS	110%	119%	128%	140%	147%	159%

It is apparent that the funding status of all these plans have improved significantly in this five-year span. Particularly noteworthy is the movement of LEOFF 1 from an underfunded position to that of a fully funded plan.

Also, of note is the sound position of the WSPRS. As of the end of 1999, the plan had a funding ratio of 159%, indicating its financial soundness.

Contribution Rate Comparisons:

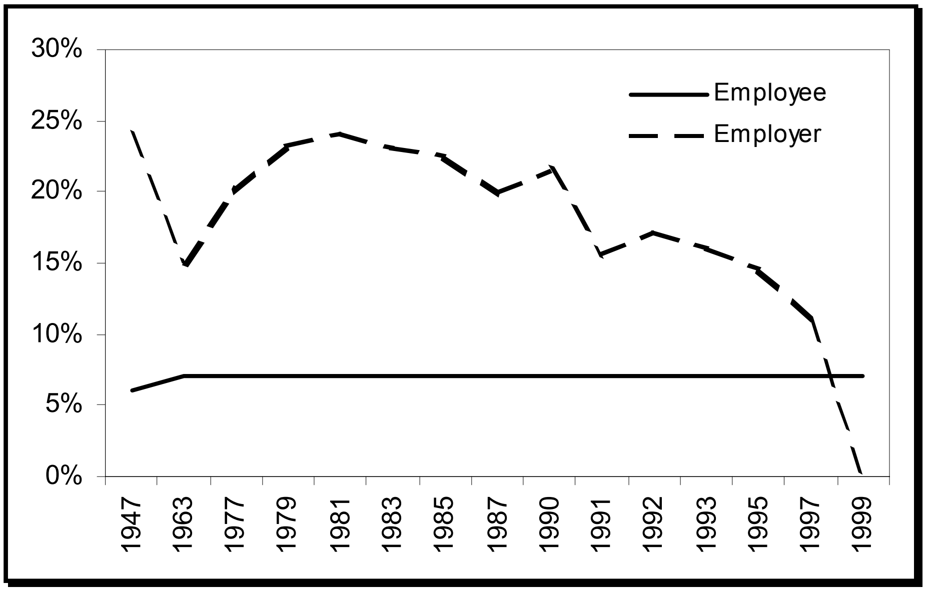
WSPRS and Plan 1 Employee Rates Fixed:

Because these retirement plans, save for the exceptions already noted, are defined benefit plans, the contributions can vary based on the financial health of the plans. In the various Plan 1 systems, the employee contributions are set in statute; for LEOFF 1, TRS 1, and PERS 1 the employee contribution rate is 6%. The employer contributions are variable based on recommendations by the Pension Funding Council.

The WSPRS employee and employer contributions are similar to the Plan 1 systems in that the employee contribution is set in statute, though at 7%. The employer contribution is "normal contribution" (i.e., normal cost) and an "unfunded liability contribution" as calculated by the Office of the State Actuary.

The net result is that the variability in funding these Plan 1 and WSPRS systems falls upon the employer or the state. While the employer and state contributions have declined markedly, it must be noted that the bulk of the contributions to these systems, up until currently, have been born by the employers and the state.

Employer and Employee Contribution Rates
WSPRS: Select Years 1947 - 1999



Contribution Rates by Plan 1 and WSP Systems: 1995-2000

Period beginning	PERS 1		TRS 1		LEOFF 1		WSPRS	
	Employee	Employer	Employee	Employer	Employee	Emp/State	Employee	State
9/1/1995	6.00%	7.42%	6.00%	12.22%	6.00%	19.22%	7.00%	14.56%
9/1/1996	6.00%	7.42%	6.00%	12.22%	6.00%	19.22%	7.00%	14.56%
9/1/1997	6.00%	7.32%	6.00%	11.75%	6.00%	15.21%	7.00%	11.05%
9/1/1998	6.00%	3.62%	6.00%	11.75%	6.00%	15.21%	7.00%	11.05%
9/1/1999	6.00%	4.41%	6.00%	8.49%	6.00%	6.00%	7.00%	0.00%
5/1/2000	6.00%	3.58%	6.00%	6.03%	0.00%	0.00%	3.00%	0.00%
9/1/2000	6.00%	4.44%	6.00%	7.10%	0.00%	0.00%	3.00%	0.00%

Note: LEOFF 1 employer contribution rate is the sum of the employer and state rate.

Comparing WSPRS and Plan 2/3 Contribution Rates:

Plan 2 and Plan 3 systems approach to contribution rates are decidedly different from Plan 1 and WSPRS. In these systems, both the employee and employer contribution rates are variable, based on equally shared costs to these systems plus, on the employer side, an accommodation of the unfunded liability in the Plan 1 systems. The net result is that employee contributions are not fixed in statute, and thus, in the most recent adjustments have fallen, again thanks to the strong actuarial performance of the systems.

Contribution Rates by Plan 2 and WSP Systems: 1995-2000

Period beginning	PERS 2		TRS 2		LEOFF 2		WSPRS	
	Employee	Employer	Employee	Employer	Employee	Emp/State	Employee	State
9/1/1995	5.08%	7.42%	6.59%	12.22%	8.41%	18.27%	7.00%	14.56%
9/1/1996	5.08%	7.42%	6.59%	12.22%	8.43%	18.29%	7.00%	14.56%
9/1/1997	4.65%	7.32%	6.06%	11.75%	8.48%	14.30%	7.00%	11.05%
9/1/1998	4.65%	7.32%	6.03%	11.75%	8.48%	14.30%	7.00%	11.05%
9/1/1999	1.85%	4.41%	2.94%	8.49%	5.87%	5.87%	7.00%	0.00%
5/1/2000	1.54%	3.58%	1.85%	6.03%	5.41%	5.41%	3.00%	0.00%
9/1/2000	2.43%	4.44%	3.01%	7.10%	6.78%	6.78%	3.00%	0.00%

Note: LEOFF 1 employer contribution rate is the sum of the employer and state rate.

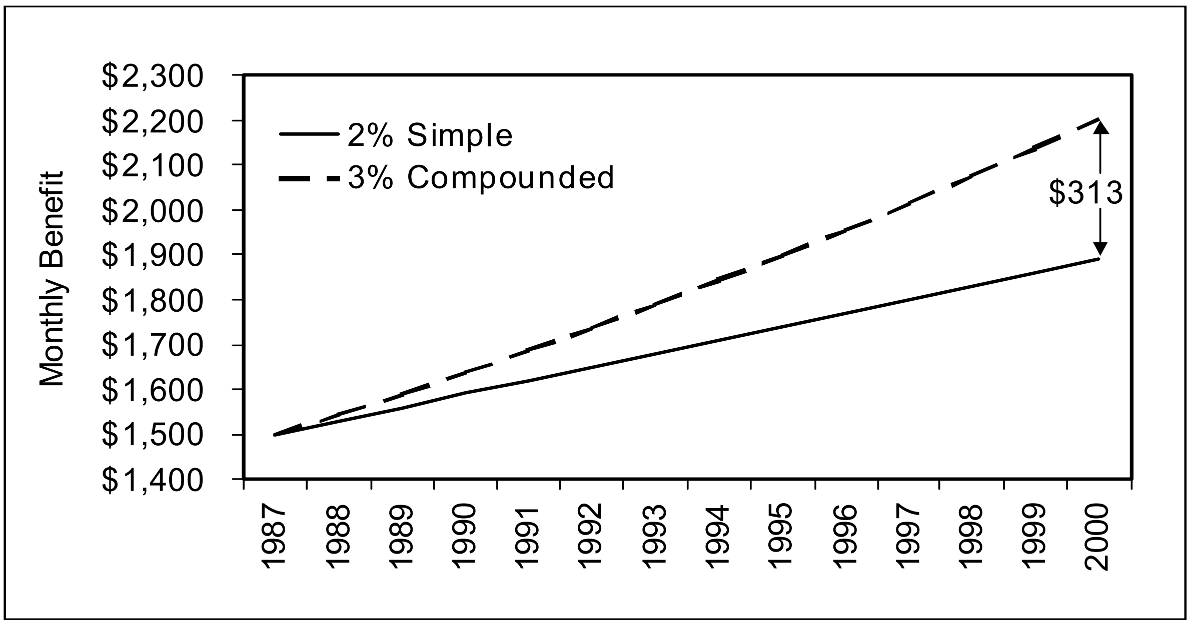
What is apparent when contrasting the Plan 1 and Plan 2 systems is that the plan 2 configurations guarantee that employee contribution rates will never be higher than the employer rate or the employer and state rate combined. And because of the Plan 2 accommodation of the unfunded liability in Plan 1, the employee contribution rates can be considerably lower than the employer rates.

Appendix D

Post Retirement Benefit Adjustments

Comparing an initial benefit of $1,500 per month adjusted by either a simple 2% COLA or a compounding 3% COLA.

The retirement allowance of those receiving a simple 2% annual cost-of-living adjustment would have increased from $1,500 to $1,890 between 1987 and 2000, a gain of 26 percent



The retirement allowance of those receiving a compounding 3% annual cost-of-living adjustment would have increased from $1,500 to $2,203 between 1987 and 2000, a gain of 46.9%.

The difference in the monthly benefits in 2000 would be $313 or 16.6%.

COLA Provisions

WSPRS Members:

Each July 1st following retirement an increase of 2 percent of the initial service retirement allowance is provided to the member.
WSPRS Survivors:

As of July 1, 2000 survivors may continue receiving the 2% COLA each July 1st if, upon retirement, an actuarially reduced benefit was chosen. Those not choosing the reduced benefit option receive the member's allowance or half the member's AFS, whichever is less, which is then adjusted by the "annual increase amount" each July 1st after the survivor reaches age 66.

PLAN 2 System Members:

Each July 1st, after one year of retirement, the member's allowance is adjusted based on the Seattle-Tacoma-Bremerton Consumer Price Index for Urban Wage Earners and Clerical Workers (CPI-W) to a maximum of 3%.

PLAN 2 System Survivors:

Plan 2 survivors receive the same COLA as retired members. Each July 1st, the survivor's allowance is adjusted based on the Seattle-Tacoma-Bremerton Consumer Price Index for Urban Wage Earners and Clerical Workers (CPI-W) to a maximum of 3%.

Washington State Patrol Retirement System
Bill Summary

Background:

The Washington State Patrol Retirement System was founded in June 1947. This system provides a retirement benefit based on a formula which multiplies the member's years of service by their average final salary (AFS) and 2%, with a maximum benefit not to exceed 75% of AFS. The WSPRS is currently the only state-administered plan that still contains many of the provisions altered or eliminated under the Plan 2/3 systems. These include:

- Disability benefits not based on service and paid from WSP operating funds.
- Two-year average final salary used in calculating retirement benefits.
- Inclusion of annual and holiday leave cash-outs in calculation of average final salary.
- Credit for prior military service at no cost to the member.
- A simple 2% post retirement COLA.
- Survivor benefits provided at no cost to the member
- A fixed employee contribution rate.

Summary:

This bill would modify the disability provisions for new members. A duty-disability benefit would be a minimum of 50% of compensation at a member's existing wage less L&I and an accrued pension. The non-duty disability benefit would be the accrued pension actuarially reduced.

The definition of "average final salary" for new members would be changed from a 2-year average to a 5-year average. For existing members the definition of "salary" would be changed to prospectively exclude voluntary over-time. For new members "salary" would exclude voluntary over-time and annual and holiday cash-outs.

The bill would change the military service credit provisions so that new members may include only interruptive service in their benefit calculations.

The bill would modify the post retirement adjustment provisions. The simple 2% cola would be changed to a CPI-based compounding COLA with a maximum of 3% per year. This COLA would apply to all existing retirees and beneficiaries.

The bill would also add new sections dealing with options for payment of retirement allowances and death benefits for new members. It would increase the minimum retirement allowance by 3% per year.

The bill would modify the survivor benefits, amending existing statutes, limiting them to existing members, and add a new section that would be more comparable to currently open plans.

Member's contribution rate would be set at 2.00% or equal to the employer rate, whichever is greater, and contribution rates would be determined by an "aggregate actuarial cost" method.

Washington State Patrol Retirement System

Sectional Analysis

Section 1: Changes the duty disability benefit for new members to include an accrued pension component and sets the benefit at a minimum of 50% of compensation at a member's existing pay.

Section 2: Changes the non-duty disability benefit for new members to an accrued pension actuarially reduced from age 55 or from when the member could have attained 25 years of service, whichever is less.

Section 3: Changes the definition of "Average Final Salary" for new members from a 2-year average to a 5-year average.

Adds a new definition of "salary" for existing members so as to prospectively exclude voluntary over-time pay.

Adds a definition for "salary" for new members that excludes voluntary overtime pay and annual and holiday pay cash-outs.

Section 4: Changes military service credit for new members to include only 5 years of interruptive service.

Changes the calculation of the post-retirement COLA from a simple 2% to a CPI-based compounding adjustment with a maximum of 3% per year and makes it available for all existing retirees and beneficiaries.

Section 5: Adds a section on "options for payment of retirement allowances" for new members.

Section 6: Amends the existing survivor benefits section to limit it to current members.

Section 7: Adds a section on death benefits for new members.

Section 8: Adjusts the minimum retirement allowance by 3% per year.

Section 9: Amends a survivor benefit options section removing unnecessary language resulting from a new section.

Section 10: Amends the funding section to use an "aggregate actuarial cost method" to determine contribution rates for the State Patrol.

Section 11: Adds a section to the funding chapter setting the employee contribution rate to 2% or equal to the employer rate, whichever is greater, and allowing for supplemental rate increases.

Section 12: Repeals now-unnecessary sections.

Section 13: Directional Instructions.

Section 14: Emergency clause and effective date.

FISCAL NOTE

REQUEST NO.

RESPONDING AGENCY:	CODE:	DATE:	BILL NUMBER:
Office of the State Actuary	**035**	**01/04/01**	**Z-0357.1/01**

SUMMARY:

This bill impacts the Washington State Patrol Retirement System by:

1. Changing the COLA from a simple 2% to a 3% CPI-based adjustment for beneficiaries as well as retirees.

2. Changing the employee contribution rate from a fixed 7% to the greater of 2% or the employer rate.

3. Excluding prospectively voluntary overtime from the definition of salary.

and in addition for members commissioned after January 1, 2003 by:

1. Changing from a 2 year to a 5 year Average Final Salary.

2. Excluding annual and holiday pay cash-outs.

3. Changing military service to include only up to 5 years interruptive military service.

4. Providing a disability benefit equal to the reduced accrued pension. (This benefit is used to offset the 50% of compensation benefit payable outside of the pension plan).

5. Removing the post-retirement death benefit and allowing the member to select an actuarial equivalent benefit option.

6. Changing the pre-retirement death benefit to return of the member's accumulated contributions for members who are single or have less than ten years of service. For married member or one with an eligible child to a reduced accrued benefit or 150 percent of the member's accumulated contributions at the survivor's option.

In addition this bill provides that the funding of the plan shall be done on an aggregate actuarial cost method, as done for other plan 2's.

Effective Date: July 1,2001.

BACKGROUND DISCUSSION:

This changes the cola to the same used in other plan 2's. This is in most cases more favorable since it provides a 3% compound cola to the member and their beneficiary instead of the current 2% simple cola to the member. Only when the actual inflation is less than 2% on an accumulative basis would this provide for less of an increase. This is also likely to provide a better cola to the beneficiary than the current uniform cola increase.

The current employee rate fixed at 7% is similar to the fixed 6% rate for other Plan 1's. The splitting of the costs is similar to the other plan 2's. The 2% rate provides that current and new member's pay for a portion of their costs.

The other changes makes this plan more similar to the Law Enforcement and Firefighter's Retirement Plan 2 (LEOFF) for those who become members after July 1,2001.

MEMBERS IMPACTED:

We estimate that all of the 968 active, 15 deferred vested, 67 disabled, and 647 retired members of this system would be affected by this bill.

1. The average monthly benefit for a new retiree in this system was $3,124 in 1999. A 2% increase would be $62.48. A 3% increase would be $93.72. The total increase over ten years would be $624.80 for the simple 2% increase. The 3% compound increase would be $1,074.40 over ten years.

2. The average salary for the active member is $57,496. Contributions at 7% would be $4,024.72. Contributions at 2% would be $1,149.92. In the very long run, if the assumptions of the plan are realized, the cost of the new member is expected to be about 16.52%. The contributions at half this rate for the member (8.26%) would be $4,749.17

3. We do not have the data to estimate the average effect of eliminating voluntary overtime. This will have an effect on individuals who have a large amount of voluntary overtime in their last two years of employment.

For new members after January 1, 2003 we estimate:

1. The change from a 3 year to a 5 year average final salary would result in an average 6% decrease in benefits.

2. The elimination of cash outs from the salary included under the plan would result in approximately an 8% decrease in benefits.

3. The change in the military service provisions would result in a decrease in benefits of 9%. (Based on an average 2.5 years of military service for someone with 25 years of service: 2.5/27.5 = 9%).

4. There is currently no disability benefit payable from the pension plan. This provides a benefit equal to the accrued pension under the plan, reduced for early commencement. This benefit is an offset to the duty disability benefit received outside the plan.

5. The post-retirement death benefit is about 7% of the total cost of the plan. This will affect married members more than this, and will not affect members without beneficiaries.

6. The pre-retirement death benefit of 50% of the member's pay is replaced with a reduced accrued benefit or 150% of the member's accumulated contributions for the married member with ten years of service, and a return of 100% of the member's accumulated contributions for those with less than ten years of service. This is a much smaller death benefit, especially for those with a few years of service and/or those who have not attained the normal retirement age.

FISCAL IMPACT:

Actuarial Determinations:

Because the assets will continue to exceed the present value of projected benefits there is no immediate impact of these changes on the employer's contribution rates.

The benefit changes to new members will not have an affect until those members enter the plan and funding commences for them. The current cost for a new member is 19.68% - 7.00% or 12.68% of pay. Under the proposed plan the expected long term cost would be about half of 16.52% or 8.26% of pay for the employer and an equal amount to the employee. However until the plan is no longer fully funded this cost will be "funded" by the surplus in the plan and the employee's 2% contribution rate.

The change in the employee rate from 7% to 2% is expected to reduce the present value of employee contributions by $27.251 million for current members. This will accelerate the time when the plan will have to resume contributions, and/or the amount of those contributions.

The bill will impact the actuarial funding of the system by increasing the present value of benefits payable under the Washington State Patrol Retirement System and the required actuarial contribution rate as shown below:

Washington State Patrol Retirement System:

(Dollars in Millions)	**Current**	**Increase**	**Total**
Actuarial Present Value of Projected Benefits The Value of the Total Commitment to all Current Members	$545	$44	$589
Unfunded Actuarial Accrued Liability The Portion of the Plan 1 Liability that is Amortized until 2024	$(213)	$44	$(169)
Unfunded Liability (PBO) The Value of the Total Commitment to all Current Members Attributable to Past Service	$(246)	$26	$(220)
Required Contribution Rate	-8.28%	-7.15%	-15.43%

As stated above it is expected that the employer contribution rates would eventually rise to +8.26% as new members are added to the plan if our valuation assumptions are realized in the very long term. Without these changes the rate would be expected to rise to +12.70%.

The chart below illustrates the effect of these changes on the contribution rates of the current membership.

	Normal Cost	Employee Rate	Employer Rate	Amortization of Unfunded	Total Employer Rate
Current Rate	19.70%	7.00%	12.70%	-20.98%	-8.28%
Increase to Cola	22.64%	7.00%	15.64%	-18.42%	-2.78%
Change in Employee Rate	22.64%	2.00%	20.64%	-18.42%	2.22%
Change to Aggregate	-13.43%	2.00%	-15.43	NA	-15.43%

The table below shows the expected long-term change in the employer cost by looking at the change in the entry-age normal cost.

Current Employer Normal Cost	12.70%
Increase for 3% COLA	2.94%
Eliminate Prior Military Service	-1.65%
Eliminate Cash Outs & "voluntary" overtime	-1.45%
Change 3YR. AFC to 5YR. AFC	-1.18%
Disability	0.10%
Death Benefits	-1.95%
Change In Employee Contribution	-1.26%
Employer Rate for New Employees	8.26%

Fiscal Budget Determinations:

Because the value of assets exceeds the present value of fully projected benefits the required contribution rate remains at zero, even without the change to the aggregate method.

Gerald B. Allard, State Actuary

STATEMENT OF DATA AND ASSUMPTIONS USED IN PREPARING THIS FISCAL NOTE:

The costs presented in this fiscal bill are based on our understanding of the bill as well as generally accepted actuarial practices including the following:

1. Costs were developed using the same membership data, methods, assets and assumptions as those used in preparing the December 31,1999 actuarial valuation report of the Washington State Patrol Retirement System.

2. As with the costs developed in the actuarial valuation, the emerging costs of the System will vary from those presented in the valuation report or this fiscal note to the extent that actual experience differs from that projected by the actuarial assumptions.

3. Additional assumptions used to evaluate the cost impact of the bill which were not used or disclosed in the actuarial valuation report include the following:

    The long term cost of the pre-retirement death and disability benefits for new members was estimated using the entry-age costs for LEOFF 2.

4. The analysis of this bill does not consider any other proposed changes to the system. The combined effect of several changes to the system could exceed the sum of each proposed change considered individually.

5. This fiscal note is intended for use only during the 2001 Legislative Session.

6. The funding method used for Plan 1 utilizes the Plan 2 employer/state rate as the Normal Cost and amortizes the remaining liability (UAAL) by the year 2024. Benefit increases to Plan 2 will change the UAAL in Plan 1. The cost of benefit increases to Plan 1 increases the UAAL.

    Costs were shown amortizing the surplus by the year 2024. Because the plan is fully funded the rate is zero and no amortization is occurring.

7. Plan 2 utilizes the Aggregate Funding Method. The cost of Plan 2 is spread over the average working lifetime of the current active Plan 2 members.

GLOSSARY OF ACTUARIAL TERMS:

Actuarial Present Value: The value of an amount or series of amounts payable or receivable at various times, determined as of a given date by the application of a particular set of Actuarial Assumptions.

Projected Benefits: Pension benefit amounts which are expected to be paid in the taking into account such items as the effect of advancement in age and past and anticipated future compensation and service credits.

Unfunded Actuarial Accrued Liability(UAAL): The cost of Plan 1 is divided into two pieces. The Normal Cost portion is paid over the working lifetime of the Plan 1 active members. The remaining cost is called the UAAL. The UAAL is paid for by employers as a percent of the salaries of all plan 1, 2 and 3 members until the year 2024.

Pension Benefit Obligation (PBO): The portion of the Actuarial Present Value of future benefits attributable to service credit that has been earned to date(past service).

Unfunded Liability (Unfunded PBO): The excess, if any, of the Pension Benefit Obligation over the Valuation Assets. This is the portion of all benefits earned to date that are not covered by plan assets.